United States Court of Appeals

for the Second Circuit

JOINT APPENDIX

DEC 10 1976
A. DANIEL FUSARO, CLERK
SECOND CIRCUIT

76-6161

United States Court of Appeals

For the Second Circuit.

SECURITIES and EXCHANGE COMMISSION,
Plaintiff-Appellee,

against

GALAXY FOODS, INC., ARTHUR LIEBERMAN a/k/a ARTY LEE, RALPH AVNI, CHARLES HOROWITZ, BRUCE KATZ, STEVEN ROTH, MARK GLAZER, IRWIN DONALD KIRSCHENBLATT a/k/a DONALD KIRSCH, GEORGE PADILLA, ARTHUR SHEVACK,
Defendants,

IRWIN DONALD KIRSCHENBLATT, a/k/a DONALD KIRSCH and ARTHUR SHEVACK,
Defendants-Appellants.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF NEW YORK.

JOINT APPENDIX.

Volume IV—Pages 1341 to 1831.

GOIDEL, GOIDEL & HELFENSTEIN, P. C.
Attorneys for Defendants-Appellants
127 John Street
New York, N. Y. 10038

WILLIAM D. MORAN
Regional Administrator, Securities and Exchange Commission, Attorney for Plaintiff-Appellee
26 Federal Plaza
New York, N. Y. 10007

THE REPORTER COMPANY, INC., New York, N. Y. 10007—212 732-6978—1976

THE COURT: Well

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INDEX TO APPENDIX.

	Page
Relevant Docket Entries	1a
Complaint	3a
Order to Show Cause Seeking Appointment of an Equity Receiver, Etc.	28a
Affidavit of Harry L. Garmansky in Support of Motion	32a
Exhibit A, Annexed to Affidavit of Harry L. Garmansky	47a
Exhibit B, Annexed to Affidavit of Harry L. Garmansky	70a
Answer	71a
Notice of Motion of Defendants Lieberman, Anvi and Glazer to Dismiss the Complaint	79a
Affidavit of Bert L. Gusrae in Support of Motion	82a
Notice of Cross-Motion of Defendants Shevack and Goidel to Dismiss the Complaint	86a
Affidavit of Arthur Shevack in Support of Cross-Motion	89a
Affidavit of Alvin I. Goidel in Support of Cross-Motion	95a
Memorandum and Order by Neaher, D. J., Denying Defendants' Motions to Dismiss	100a
Order of Preliminary Injunction Against Defendants Shevack and Kirsch	112a

Page

Transcript 1

Opening Statement by Mr. Garmansky 5

Opening Statement by Mr. Goidel 10

Opening Statement by Mr. Padilla 14

Motions 1467, 1657

Plaintiff's Findings of Fact and Conclusions of Law 1663

Defendants Shevack and Kirsch's Findings of Fact and Conclusions of Law 1740

Memorandum Decision Permanently Enjoining Defendants 1756

Final Judgment of Permanent Injunction Against Defendants Shevack and Kirsch 1826

Notice of Appeal 1831

TESTIMONY.

WITNESSES FOR PLAINTIFF:

Beck, Howard Ray:

Direct by Mr. Lerner 881

Cross by Mr. Goidel 931

Cross by Mr. Padilla 999

Redirect by Mr. Lerner 1006

Recross by Mr. Goidel 1014

Redirect by Mr. Lerner 1016

Deceglie, Paul John:

Direct by Mr. Garmansky 1017

Cross by Mr. Goidel 1096

Cross by Mr. Padilla 1106

Page

Kirschenblatt, Irwin Donald:

Direct by Mr. Lerner 25

Cross by Mr. Goidel 201

Cross by Mr. Padilla 229

Redirect by Mr. Lerner 234

Recross by Mr. Goidel 260

Recross by Mr. Padilla 261

Lieberman, Arthur:

Direct by Mr. Garmansky 22

Recalled:

Direct by Mr. Garmansky 263

Cross by Mr. Goidel 433

Cross by Mr. Padilla 632

Redirect by Mr. Garmansky 721

Redirect by Mr. Lerner 761

Recross by Mr. Goidel 847

Recross by Mr. Padilla 869

Redirect by Mr. Lerner 872

McLean, Melvin J.:

Direct by Mr. Garmansky 1207

Cross by Mr. Goidel 1260

Cross by Mr. Padilla 1297

Page

Silverman, Georgette:

Direct by Mr. Garmansky 1400

Cross by Mr. Goidel 1415

Silverman, Steven:

Direct by Mr. Garmansky 1304

Cross by Mr. Goidel 1354

Simmons, Branch:

Direct by Ms. Mysliwiec 1108

Cross by Mr. Goidel 1151

Redirect by Ms. Mysliwiec 1189

WITNESS FOR DEFENDANTS' SHEBACK AND KIRSCHENBLATT:

Shevack, Arthur Craig:

Direct by Mr. Goidel 1468

Cross by Mr. Garmansky 1532

Redirect by Mr. Goidel 1652

EXHIBITS.

PLAINTIFF'S EXHIBITS:

		Admitted Page	Printed Page
1.	Certificate of Non-Registration .	21	1832
3.	Galaxy Business Manual (Vol. 1, No. 111)	307	1833
7.	Newspaper advertisement . . .	73	1856
8.	Application and Agreement (blank)	75	1858
10.	Memo from Kirsch	251	1861
11	for Identification. "It's Your Move" Galaxy Binder	274	1862
12.	Outline of Training Session . .	382	1885
15.	Galaxy newspaper advertisement, August 1, 1972	824	1888
16.	Newspaper advertisement, August 20, 1972	827	1889
17.	Galaxy Article, undated . . .	830	1890
20.	Application of Kunst . . .	797	1891
21.	Galaxy Brochure	805	1898
26.	Galaxy flyer	888	1899
27.	Application of Beck	903	1902
28.	Wage and Tax forms of DeCeglie .	1020	1905
32.	Invitation card	1211	1915

	Admitted Page	Printed Page
35. Application of Silverman . .	1316	1916
38. Manufacturers forms	1344	1919
39. Family Finance forms . . .	1344	1928
44. Futuristic Contract	1647	1938

DEFENDANTS' EXHIBITS:

E. Memo from Kirsch	529	1945
G. Letter from Silverman, December 29, 1972	604	1947
J. Galaxy Corp. Records	659	1948
P. Galaxy Balance Sheets . . .	867	2001
Q for Identification. Shareholders Agreement	1299	2005

MR. GOIDEL: I agree with what your Honor has said --

THE COURT: Your objection must be very subtle because to me --

MR. GOIDEL: Your Honor has said that I would have a right to cross-examine. That is what your Honor said, on the basis of these documents, and I agree. All I am saying is that I do not have somebody from Family Finance or whatever organization --

THE COURT: Yes, my point is it is not incumbent on the proponent of the record to call the witness unless you insist on the technical objection which is that the witness who appears says I work in the loan application department and it is the regular course of business in that department to make it keep records of loan applications and other data respecting same.

"I have with me the records which pertain to the loan application of Stephen Silverman."

"Did you work on the application?"

"No, I did not."

"How did you happen to get this batch of records?"

They were handed to me by my supervisor. I was told to bring them to court. But I do know that

these are records that were normally kept and made in the regular course of business. Although we have 16 record keeping clerks, I am one of the 16 and I did not happen to work on this."

Now, that is as admissible as anything could be for the contents it contains, whatever. That is the way I understand the shop book rules.

MR. GOIDEL: And I agree with you. But my understanding is, and perhaps I am in error and if I am in error I certainly will stand corrected, but everything your Honor has said is accurate. But your Honor is carrying this I believe at least one step further --

THE COURT: My point is there is testimony here about your client's statement to utilize this and so forth. Your client may say to you, "That is all poppycock." I don't know. "There is not a grain of truth in it." So what should you do? You call up Household Finance or Family Finance and you can bring a witness down here or try to find out who in that company did in fact work on the investigation of that. Then you get him to say that I was hoping to call him up but I just checked it off anyway. Then you have rebuttal. But up to that point it is a box which says

"Employment verified" or words to that effect. And that is what you are up against. But that was done. There was reliance, in other words, upon a statement which recalls or which is presumed on the basis of the witness' testimony.

MR. GOIDEL: All right, not to belabor the point any further and not trying to be very subtle, I withdraw my objection to the introduction of these docjments. I may, however, your HOnor ask time then to have subpoenaes issued if it becomes necessary as it relates to some of the information contained therein.

THE COURT: You certainly have the right, as I said, to have anybody that you wish.

MR. GOIDEL: Are you going to use these right now in your questions (addressing Mr. Garmansky)? Well, you were going to put them in evidence.

MR. GARMANSKY: Yes.

MR. GOIDEL: I want time to read them.

MR. GARMANSKY: Surely.

THE COURT: So these are going in evidence then, is that right?

MR. GARMANSKY: Yes your Honor.

THE CLERK: Plaintiff's Exhibits 38, 39 and 40

now marked in evidence.

(Documents referred to were thereupon received and marked Plaintiff's Exhibits 38, 39 and 40 respectively in evidence.)

BY MR. GARMANSKY:

Q Mr. Silverman, did you receive any money from these loan applications that you made?

A Yes, I did.

Q Approximately how much money did you receive?

A It was approximately $6200 or $6300, $6000, around there.

Q Did you get this money all at one time?

A No I did not.

Q How long a period of time did you get this money?

A It was within a short period of time. I would get the check and I would sign it over to Mr. Shevack.

THE COURT: What did you do? You endorsed it over to him?

THE WITNESS: Yes.

THE COURT: Well you said I signed it over.

What do you really mean? Are you familiar with an endorsement on the back of the check.

THE WITNESS: Yes, I endorsed on the back.

THE COURT: Pay to the order of Shevack or somebody else?

THE WITNESS: Well, when I had handed him these checks which were to go into the company he had given me a receipt in return for the checks which I was giving for the purpose of joining Galaxy.

THE COURT: So you got his receipt.

THE WITNESS: Yes I did.

THE COURT: These checks of course were made to your order, or to your order and your wife's order.

THE WITNESS: Yes, they were made to --

THE COURT: You simply signed your name on the back.

THE WITNESS: Yes I did.

MR. GARMANSKY: I would like to mark at this time a one page document with handwriting on it. It is Plaintiff's Exhibit what?

THE CLERK: 41, coming up.

So marked Plaintiff's exhibit 41 for identification.

(Document referred to was received and marked Plaintiff's Exhibit 41 for identification.)

Q Mr. Silverman, do you recognize what has been marked as Plaintiff's Exhibit 41?

A Yes I do. That is the receipt handed to me which Mr. Shevack kept the records as the checks I was giving him.

Q This Plaintiff's Exhibit 41 is one receipt or more than one receipt?

A Excuse me?

Q Is it one receipt or more than one receipt?

A It is one receipt.

Q What is the date of the receipt?

A 10/17/72.

THE COURT: Does that cover the entire --

THE WITNESS: I assume here on the bottom --

THE COURT: No, you can't assume anything.

THE WITNESS: Oksy.

THE COURT: You have identified it. Is there some question about the date.

THE WITNESS: No, you see as I handed him the check he put the date down. That is the date I was looking at. The entire amount that was received was received on October 26, 1972.

THE COURT: So between the 17th and the 26th both checks were sent over.

THE WITNESS: Yes.

Q Did you see Mr. Shevack sign Plaintiff's Exhibit 4

Mr. Silverman.

A Yes I did.

Q Did Mr. Shevack give you Plaintiff's Exhibit 41?

A Yes he did.

MR. GARMANSKY: I would like to offer into evidence Plaintiff's Exhibit 41.

MR. GOIDEL: I have no objection.

THE CLERK: Plaintiff's Exhibit 41 now marked in evidence.

(Document referred to having previously been marked Plaintiff's Exhibit 41 for identification was now received and marked Plaintiff's Exhibit 41 in evidence.)

Q Mr. Silverman, did you have any discussions with Mr. Shevack about using six banks and finance companies?

A Well, as I stated before he said that I would -- I probably wouldn't be able to get the full amount in one bank and therefore went around to the different banks to obtain the cash.

Q And did Mr. Shevack give you any instructions concerning the various banks and finance companies that you went to other than what you just testified to?

A I am not sure I understand your question.

MR. GARMANSKY: I will rephrase the question.

8 Silverman

THE COURT: Well, are we exploring whether he filed some others that were turned down? Is that the point?

Q Mr. Silverman, did Mr. Shevack instruct you concerning any outstanding loans that you had?

THE COURT: First of all did you have any outstanding loans.

THE WITNESS: No -- he told me when I went to fill out applications not to say that I had any loans with anyone else or I probably wouldn't be able to get the amounts.

Q How about making applications with other banks, did he instrudt you as to that?

A Well, I did make applications with other banks and certain banks did turn me down.

Q Did he give you any instructions as to what to tell other banks after you had left one bank?

A Just that I hadn't taken out any other loans.

Q Now, Mr. Shevack on these that you filled out -- Mr. Silverman, on these loan applications you filled out --

THE COURT: Do I understand you to say that although you made three applications which were granted --

THE WITNESS: Four.

THE COURT: Four were granted.

THE WITNESS: Yes sir. Family Finance, Household Finance and Manufacturer's --

MR. GARMANSKY: We only have three of the applications.

THE COURT: Oh, I see. There was another one?

THE WITNESS: First National City.

THE COURT: So it was two banks and two --

THE WITNESS: Yes.

THE COURT: So do you mean that when you applied to each of these institutions separately you did not mention you were also applying to the others?

THE WITNESS: No, that is correct.

THE COURT: What is correct?

THE WITNESS: That I had not said that I had applied with other banks.

THE COURT: So far as each bank was concerned they were unaware that other banks were considering your applications and making loans to you?

THE WITNESS: Yes sir.

Q Mr. Silverman, was anyone instructing you to do that?

A Yes, Mr. Shevack said that would be the only way I would be able to get the money. That would be the only way I would be able to get the necessary cash.

Q Mr. Silverman, you testified you invested $7000 in Galaxy?

A Yes I did.

Q From what source did you get the other funds?

A Well, approximately, as I said, $6200 to $6300 was from the actual loans, the amounts they paid to me, the banks, and I had a small amount in the bank, a few hundred in the bank, which I had taken out. Mr. Shevack had lent me the remainder of $300.

THE COURT: Just to make up the $7000?

THE WITNESS: Yes, to be paid back whenever I made money in Galaxy.

Q Now, Mr. Silverman, have you paid off these loans since you first obtained them?

A Approximately two thirds of the loans have been paid.

Q Have you ever defaulted on any?

A No.

MR. SILVERMAN: After you joined Galaxy in around October, 1972 did you earn any money?

THE WITNESS: No I did not.

Q Did you request a refund of that money?

A Yes I did.

Q Did you receive that refund?

11 Silverman

A No I didn't.

MR. GARMANSKY: Your Honor, we have no more questions of Mr. Silverman.

MR. GOIDEL: Your Honor, don't you need a little time to read these documents.

THE COURT: Well, how about if I give you until 4:00 o'clock here.

MR. GOIDEL: Fine.

MR. GARMANSKY: We have one other witness today. And after that one witness the Commission will rest. That is Mrs. Silverman, and not a long witness at all.

THE COURT: Well, we would probably take a break now anyway. So I'm going to give Mr. Goidel about 18 minutes to review the documents.

THE WITNESS: She will be coming on?

MR. LERNER: Not now. It will be a good hour.

THE COURT: Do you expect that much cross-examination.

MR. LERNER: I imagine.

THE COURT: Well, is there somebody else here?

MR. LERNER: His wife.

THE COURT: Well, I will be back at 4:00 o'clock.

(Recess.)

(Continued on next page)

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MR. GARMANSKY: Your Honor, I forgot to ask two questions.

THE COURT: Go right ahead.

DIRECT EXAMINATION

BY MR. GARMANSKY: (Cont.)

Q Mr. Silverman, did there come a time when you came to the Securities and Exchange Commission to explain to us what you just testified to?

A Yes.

Q Do you recall when this was?

A Not exactly.

Q What was the year?

A The year?

Q Yes.

A (No response.)

Q The first time?

A The first time was I had gone to the Consumer Affairs and the SEC. It was probably '73, 1973.

Q When you explained the bank loans to the Securities and Exchange Commission, what did we tell you concerning that?

A That it was the wrong thing to have done.

Q Did we tell you you may have committed an illegal act?

A Yes.

Q In exchange for your testimony here today did the Securities and Exchange Commission give you any promises or anything whatsoever?

A No.

MR. GARMANSKY: Thank you.

Your witness.

THE COURT: All right.

CROSS-EXAMINATION

BY MR. GOIDEL:

Q I show you plaintiff's exhibit 57, would you look at it?

A Yes.

Q Were you present when that was written?

A Yes.

Q Where was it written?

A Where was it written?

Q Yes.

A Exactly where it was written I cannot honestly recall. I was with Mr. Shevack and my wife at a time when he had written this.

Q I think you said it was given to you in the car? Is that correct?

A Yes, I believe so.

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Q Do you believe so sir, or do you know so?

A I believe so. I am not exactly 100 percent sure when it was given to me. It is two years old. I was there.

Q Could it have been given to you somewhere other than inthe car?

A Well, he had handed me the W-2 form at the time I can't swear to it 100 percent he gave me this the exact time.

Q Were you there when it was written?

A Yes I was.

Q Now, I think you said that Mr. Shevack picked you up in a car?

A Yes.

Q He drove over to you?

A Yes.

Q And picked you up?

A Yes.

Q Did he hand that to you while he was driving?

A I believe -- well, when he handed me the W-2 form he had handed me this statement.

Q Was he driving at the time?

A Was he driving?

Q Yes.

A When we had gotten to the bank.

Q When you had gotten to which of the banks?

A It had to be the first one because when I went into each bank I presented the W-2 form.

Q Did he hand it to you while inthe car?

A Yes, he must have. Yes.

Q Please, will you bear with me for a moment. If you don't know, say so, don't guess. I want you to be as accurate as possible.

A I am trying to be.

Q Fine. If you don't know an answer, say you don't know.

Was he driving the vehicle? Had he stopped the vehicle? Had he parked the vehicle? Tell me exactly what was happening at the time he handed this to you?

A We got to the bank. He stopped the car, shut off the motor, handed me the W-2 forms and handed me this.

Q All of you were in the car at the time?

A By all, you mean --

Q You, your wife and he?

A And Peter.

Q The four of you were in the car?

A Yes.

Q Now, when did he write it?

A He wrote it while he was sitting in the car

Q It wasn't that he merely handed it to you after he parked the car but he also sat there and wrote it out, is that your testimony?

A Yes.

Q Where were you seated and where was he seated.

A He was seated in the front with his associate and I was sitting in the back with my wife.

Q Was he sitting behind the wheel of the car?

A Yes.

Q While he was seated behind the wheel of the car that's when he wrote that?

A Yes, it was.

Q That is the same person, sir, who wrote this out, that is plaintiff's exhibit 41, is that correct

A Yes.

Q So that the handwriting on both exhibits should be the handwriting of the same person, is that correct?

A Yes.

Q Is anybody else's handwriting on the first exhibit that I showed you, number 37?

A Yes.

Q Who else's handwriting is on exhibit 37?

A My wife's.

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Q What is written there in your wife's hand writing?

A Immediate supervisor, Francis Alexander.

Q Your wife write that?

A Yes.

Q When did your wife write that?

A After Mr. Shevack told her to write it.

Q Were you all still in the automobile?

A Yes.

Q In other words, when Mr. Shevack handed that paper he wasn't satisfied that your wife had enough information, is that it?

MR. GARMANSKY: Objection, your Honor. Mr Silverman does not know what went on in the mind of Mr. Shevack.

MR. GOIDEL: That is proper, withdrawn.

Q Sir, was your wife still seated in the same position when she wrote that?

MR. GARMANSKY: Objection, it hasn't been established where she was seated.

Q Was she in the back?

A Yes.

Q Was she still seated in the back when she wrote that?

A Yes.

Q Did she use the same pen?

A I can't honestly say for sure whether she did or not.

Q When Mr. Shevack handed that to you what did you say to him?

A We had discussed that previously when he had handed me the W-2 form, I told him that I didn't like the idea and my wife said she didn't like the idea either.

Q Let me ask you, I thought that the W-2 form was handed to you at the same time the paper was handed to you?

A He had told us he made up the W-2 form for us and when he told us that, that's when we started arguing about the W-2 form.

Q When did he first speak to you about the W-2 form?

A He started speaking to us about it -- it was either -- I can't honestly say, either it was the night before when I had spoken to him but he had handed it to us on the way to the bank.

Q Both documents were handed to you in the car at the same time but whether you began to argue with him about the W-2 form that day or the day earlier, you are not certain?

MR. GARMANSKY: Objection, that is not what the witness testified to.

MR. GOIDEL: I think that is.

MR. GARMANSKY: He said he began arguing with Mr. Shevack the day when Mr. Shevack picked him up and drove him up to the first bank. He could not be sure whether the W-2 form was discussed the night before or the first time the next day. He is sure he was given the W-2 form the day Mr. Shevack drove him to the bank.

A Yes.

Q The first time however that you discussed the W-2 form, or the earliest the W-2 form could have been discussed was the day before, is that correct?

A Yes.

Q Would you please tell us, and please be as precise as possible, please tell us everything that was discussed concerning the W-2 form both by you, Mr. Shevack, and even your wife?

A Fine. To the best of my recollection, since it was two years ago, Mr. Shevack had told us that we wouldn't have any problems, as I said, obtaining the loans if we would give this W-2 form stating that my wife is working for this place, A & M Dental Labs. We didn't like the idea at

all. And I asked him if there was any way I could get in trouble by doing this and he said that I shouldn't worry about it because he had done it before and that is basically the story.

Q Did you give Mr. Shevack any information at that time? Did you assist him in the preparation of the 1-2 form?

A No.

Q Did you assist him by furnishing information or actually typing it out?

A No.

Q Or any way whatsoever?

A No.

Q Did your wife?

A No.

Q Were you present when your wife was present in these discussions with Mr. Shevack or was there any time that your wife was not with you?

A No, she was with me.

Q You are certain that you never assisted Mr. Shevack in any way in the preparation of that document?

A Yes.

Q Yes, you are sure?

A I did not prepare that document in any way

Q Either by furnishing information or by physical work?

A Yes.

Q When you first met Mr. Shevack, was your wife present?

A Yes, she was.

Q I think you testified that your wife had earlier spoken with someone, whether it be Mr. Shevack or some other person associated with Galaxy, and you learned of the corporation through her?

A YEs.

Q Had she met with that person privately, if you know?

A No.

Q She had not?

A No.

Q Okay. Now, at that time your wife was not employed?

A Correct.

Q Prior to that time had your wife ever been employed?

A Are you referring to this company in particular?

Q Any company.

A She was going to school at the time.

Q She was a student?

A Yes.

Q What school?

A Kingsborough Community College.

Q You did have some feelings at the time that there might be an impropriety with what you might be requested to do?

A Yes.

Q Did you bother to consult with anybody to determine whether you were in fact committing an impropriety?

A No, I did not. I felt that I would be able to pay back the loan and Mr. Shevack said that the price would be going up in the company. They were always raising the prices and if I didn't do it, I wouldn't be able to get into Galaxy before they raised the fee.

Q When you went into the first of the lending institutions, first, can you tell us which was the first of the lending institutions you went to?

A I think -- I can't honestly say which one was first. There were approximately six that I did go to.

Q But which is the first that you do recall going to, whether it is actually number 1 or just tell me which is the first you recall going to?

A It may have been the First National City,

then again --

MR. GARMANSKY: Objection. The witness testified he could not recall. Mr. Goidel is harassing him. That answer should not stand in the record unless the witness is absolutely certain.

THE COURT: He doesn't have to be absolutely certain, it only has to be his best recollection.

Q It may not have been the first, do you recall it being the first or the second?

MR. GARMANSKY: Or the last?

MR. GOIDEL: I am trying to elicit facts. I want to see how accurate his memory is.

THE COURT: Would it help to try to recall where the various institutions were located?

THE WITNESS: A few in Manhattan and a few in Brooklyn. Again, to almost all of these -- I had never done this before anyway.

THE COURT: What is your best recollection? That you went to Brooklyn first?

THE WITNESS: I would -- I went to Brooklyn first because I live in Brooklyn.

THE COURT: Where is the First National City located?

THE WITNESS: In Brooklyn.

THE COURT: So that is your --- that is your present recollection? That's the best you can recall now, you went first to the First National City Bank in Brooklyn?

THE WITNESS: Yes.

THE COURT: Is that the nearest bank to where you started out from?

THE WITNESS: I would say so.

THE COURT: Your home was --

THE WITNESS: In Brooklyn.

THE COURT: You started out from your home?

THE WITNESS: Yes.

BY MR. GOIDEL:

Q Who went into the bank or the lending institution?

A I went in and my wife went in.

Q Anybody else go in with you?

A No.

Q Sir, I'm going to show you exhibit 38 and I am calling your attention specifically to the -- the paper referred to as comaker's statement. Do you see that, sir?

A Comaker's statement, yes.

Q Do you recognize the handwriting?

A Yes, I do.

Q Whose handwriting itis it, sir?

A It is my wife's.

Q You are familiar with your wife's handwriting?

A Ye

Q Now, sir, taking it line by line, tell me which statements contained in that application or that comaker's statement you know to be false?

A The part where she has written down where she worked, A & M Dental Labs, the address. I don't know if that is the address of that place, but that part is false.

Q Anything else on that statement false?

A Well again, only referring to A & M Dental Labs, that she is a technician working there. I can't even read it.

Q Is there anything else on the statement false?

A The amount of money she was making.

Q Now, sir, take your time. Is any other statement on that false?

A Not that I see.

Q Is there anything that you question the truth of?

A (No response.)

THE COURT: Is there anything there about other loans?

THE WITNESS: No. It all looks okay to me.

Q Do you know your wife's social security number?

A No.

Q Pardon me?

A No, I don't.

Q Do you know whether the social security number appearing, 063-38-0248 is hers?

A No, I do not.

Q That does appear in your wife's handwriting, is that correct?

A Can you show me where it is, please?

Q Yes sir.

A As I said, this number doesn't mean anything to me because I don't know anything about it.

Q It is the same number that appears on the W-2 form that is marked as Plaintiff's exhibit 36, isn't that correct?

MR. GARMANSKY: The record will speak for itself.

Q It is, take my word for it.

A Yes.

Q Now, sir, if this number here is accurate, and if it appears on the W-2 form, then would you say that either you or your wife assisted in the preparation of this document

known as the W-2?

MR. GARMANSKY: Objection, your Honor.

THE COURT: No, I will overrule the objection.

THE WITNESS: Can you repeat the question?

(Whereupon, the last question was read by the reporter.)

MR. GARMANSKY: Your Honor, his question includes the word accurate. His testimony has been he doesn't know what his wife's number is. I object to the form of the question.

THE COURT: The question is assuming it to be in fact your wife's number for the purpose of this answer, not saying it is. If it should turn out to be your wife's number would you then say neither you nor your wife aided in the preparation of the two forms?

MR. GARMANSKY: That is an inference which does not necessarily follow. Mr. Shevack may have had access to the original form.

THE COURT: But this witness is supposed to have some knowledge about his own personal family connection with the social security number. He indicated he is unfamiliar with his wife's number. If his wife later agrees that it was her number, then --

MR. GARMANSKY: I still don't follow. Mr. Shevack may have gotten that number from any source.

THE COURT: He may have --

MR. GARMANSKY: The question should be, do you know if your wife --

THE COURT: Cross-examination isn't as straightforward as direct examination. Part of it is to confront the witness with certain inconsistencies and call upon him to make an explanation. That is the purpose of cross-examination. To test the credibility of a person.

(Continued next page.)

4pm24

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4pm2

18 Silverman-cross/Goidel

MR. GARMANSKY: I don't see how it is going to test his credibility if he calls --

THE COURT: The witness already stated, I believe, neither he nor his wife aided in the preparation of either of these two exhibits.

MR. GARMANSKY: That is not the testimony. It was the W-2 form which he testified he did not aid in. That is my entire point.

THE COURT: I stand corrected. I meant that. I think I got confused because there was another document. The comaker's statement which I believe revealed the social security number.

MR. GOIDEL: They both do.

THE COURT: Which?

MR. GOIDEL: Both revealed it.

THE COURT: The comaker form, through that you determined that the social security number on the W-2 form is the same as on the comaker bank form, it would appear that the wife wrote out --

MR. GOIDEL: Yes sir.

THE COURT: Of course, the question really is whether all the wife did was copy a social security number as it appeared on the W-2 form.

MR. GOIDEL: It might well be.

THE COURT: Or in fact has such a number which she supplied to Shevack --

MR. GOIDEL: Or she did not supply to Shevack but prepared the W-2 statement herself.

MR. GARMANSKY: She may have. She can testify to that.

MR. GOIDEL: I am examining this witness. You put this witness on first.

MR. GARMANSKY: This witness can't testify to an inference. On the question of whether the wife gave the social security number and whether this is the wife's handwriting. The two put together don't mean, because her social security number appeared there that she aided Mr. Shevack in this --

MR. GOIDEL: I am trying to elicit facts. The testimony has been Mr. Shevack prepared this W-2 form.

THE COURT: Completely as it is.

MR. GOIDEL: Pardon me?

THE COURT: Completely as it is.

MR. GOIDEL: That he prepared it unaided and abetted by the parties, by this gentleman and by his wife. That's what he testified to.

Now, if this should develop to be his wife's social security number we have not yet established it

is or not, if it develops that it is, obviously something is wrong with someone's testimony so far.

MR. GARMANSKY: That doesn't follow. He may have gotten the social security number from any number of sources.

MR. GOIDEL: I would like to know what source?

MR. GARMANSKY: Ask his wife.

MR. GOIDEL: I will. But he is on the stand now.

MR. GARMANSKY: Ask him where he got the social security number.

THE COURT: He testified he is not familiar withthe number. Now you are saying if it should happen to be his wife's number -- well, I see, I think in reconsidering the commission's objection, I see more merit to it than I did at first. You are asking him in effect, as I see it, for an opinion virtually as to whether or not he would still maintain that neither he nor his wife aided in the preparation of the W-2 form even if it turned out to be actually his wife's social security number. Since he is unfamiliar with that number, the way I see it it is an argumentative question.

MR. GOIDEL: I think we lost track of it.

THE COURT: I think it is pretty clear.

MR. GOIDEL: Since he already testified neither he nor his wife did assist in the preparation of the document, if it turns out that the two numbers are correct, that they are his wife's number, would he then alter his testimony in any way and state that either he or his wife did assist inthe preparation of that document? That calls for a factual statement, not an opinion.

THE WITNESS: I can answer that. The answer is no. I had nothing to do with the W-2 form whatsoever.

BY MR. GOIDEL:"

Q What did you call your wife? Does she have a nickname?

A Yes.

Q What did you call her?

A Gigi.

Q Is that the name friends and relatives and everybody including you refer to her as?

A I am separated from my wife right now. I don't call her anything really.

Q I am sorry about your matrimonial difficulties, but for the fact that you are separated, when you were living together you called her Gigi and what did the other friends

and relatives call her generally, Gigi?

A Some Gigi. some called her Georgette, some called her George, and some called her other things.

Q What did Mr. Shevack call her?

A Georgette.

Q Is that how she was introduced to him?

A Yes.

THE COURT: Which is her proper name?

THE WITNESS: Yes.

Q Now, you say that you were told by Mr. Shevack that when you went into the bank you should forget about mentioning to whichever one you happened to be in the fact that you had applied for loans in others?

A Yes.

Q I assume that you followed his suggestion?

A Yes.

Q You did not mention to any other institution that you had applied -- made a loan from a prior one, is that correct?

A Yes.

Q Any exceptions to that?

A No.

Q Sir, I show you the application submitted to the Family Finance Company, plaintiff's exhibit 39, would you

look at that page, sir?

A Yes sir.

Q Does that bear your signature?

A Yes.

Q Is there any reference made there to any other financial loans made by you?

A Any other debts do you say?

Q Any other loans.

A Any other loans?

Q Yes. Household Finance is right down there, is it not?

A Yes.

Q Is that the loan you made from Household Finance in order to purchase an interest in Galaxy?

A This is a loan from Family Finance.

Q The reference that you have here to Household Finance, is that a reference to a loan which you took out for the purchase of Galaxy interest?

A Yes.

Q So that in contravention to the instructions or advice that was given to you by Mr. Shevack you did notify that institution at least of the existence of another loan?

A Yes.

Q Sir, would you tell us if you were following

Mr. Shevack's instructions, why did you notify this institution of the fact that you had taken a loan out from another institution?

A Sir, to the best of my recollection, when I had gone in here, into Household Finance, I believe as I state to the best of my recollection, they had a report already that I had taken out a loan from Household Finance. This is to the best of my recollection. That's why I had to put it down on the application.

Q Perhaps this helps you orient yourself into some reasonable way of determining where you went first.

Obviously it couldn't have been Family Finance that you went to first, is that correct?

A I didn't say I went --

Q I didn't say that you said it, I am asking if you are assisted in recalling where you went to first?

A No.

Q It certainly wasn't this institution because you had already gone to Household Finance, is that correct?

A I would say yes.

Q And you say that they had a report indicating that you had taken out a loan from Household Finance?

A Sir, I am not familiar with the procedures of other financial companies.

Q Look, sir, we are talking facts and you made some serious statements concerning an individual and I want to know how accurate you are. You have been inaccurate at least on this occasion, is that correct?

MR. GARMANSKY: Objection, your Honor. Mr. Goidel wants to bring out facts, let him bring out facts. Don't let the witness characterize his own testimony.

MR. GOIDEL: I am asking him if he was inaccurate in his prior testimony.

THE WITNESS: My prior --

MR. GARMANSKY: His prior testimony wasn't that he followed Mr. Shevack's instructions in every instance.

THE COURT: I will overrule your objections and let the witness answer. I think he was about to give an answer.

A As I said, this goes back two years ago. Whether I went to this bank first or another one first, even if he shows it to me here I still don't remember it, whether it was this one we went into first or that one, that's all I'm trying to say.

THE COURT: Sometimes your recollection can be refreshed by seeing something, and counsel's question

is directed really to that. That if when you went to Family Finance you have a recollection of being told that they already had a report of a loan issued to you by Household Finance. Then number 1 you must have gone to Household Finance first. Or that report would not have been possible. And secondly, that as you said was the reason why you mentioned Household Finance in applying for this family loan. Do you agree with that?

THE WITNESS: Yes.

THE COURT: I take it when you went to Household, you walked out with a loan, is that correct?

THE WITNESS: Yes.

THE COURT: Walked in with an application and walked out with a loan?

THE WITNESS: YEs.

THE COURT: And Family was operated on the same basis? Or did they take time?

THE WITNESS: They all -- they didn't just hand me a check in any of the cases, but I didn't have difficulty.

THE COURT: You didn't get the check the same day?

THE WITNESS: Yes, from Household we got the

supply it.

check the same day. You see, your Honor, as I stated when I had gotten the checks I was signing them over to Mr. Shevack.

THE COURT: I understand that. Was Household also in Brooklyn?

THE WITNESS. Household was in Brooklyn.

THE COURT: Was Family in Brooklyn?

THE WITNESS: I believe so. I really can't say for sure, yourHonor.

THE COURT: Do you have some further questions for this witness?

MR. GOIDEL: Yes, I am just trying to compare certain documents.

Your Honor, may I call for the production of at least a copy of the subpoena that was served on Household Finance?

THE COURT: Isn't it attached to the group of documents?

MR. GOIDEL: There is a letter attached.

MR. GARMANSKY: The one attached, Mr. Goidel.

MR. GOIDEL: Is there --

MR. GARMANSKY: That is not the one.

(Pause.)

Q Now, sir, I think you said that the reason why

you divulged this earlier loan to Family Finance is because they had a record of it, is that correct?

A Yes.

MR. GOIDEL: Your Honor, I submit that the subpoena called for any and all records including but not limited to loan applications, loan documents, internal bank memoranda and documents related to Mr. Steven Silverman, etcetera. The response from the attorney indicating that all records on file were furnished pursuant to the subpoena -- that is the letter of Mr. Julius Winn, apparently the attorney for the finance company.

Would you show me if there is a document if you are referring to anything specific, is that document that you were referring to --

THE COURT: He didn't refer to a document.

THE WITNESS: I said to my recollection.

THE COURT: That could have been by telephone

MR.GOIDEL: I'm sorry.

BY MR. GOIDEL:

Q Did you see a report?

A No.

Q Did somebody tell you there was a report?

A Going back, well, I can't assume here but to th

best of my knowledge, I would say there had to be a report.

MR. GARMANSKY: Objection and I move that the witness' testimony be stricken.

THE COURT: It is obviously an assumption and I will grant your application to strike it.

You saw no report?

THE WITNESS: That is correct.

THE COURT: But obviously had information. Do you have any idea how they got the information?

THE WITNESS: No, your Honor.

THE COURT: All right. That is the way you understand it?

THE WITNESS: Yes.

(Continued next page.)

4pm3

30 Silverman-cross/Goidel

MP:ss
4pm3

CROSS-EXAMINATION

BY MR. GOIDEL: (Cont.)

Q But it is your testimony, sir, you do know they already had the information? Or is that too conjecture?

A I don't like to assume.

THE COURT: You are only supposed to answer to the best of your recollection. If you have no recollection on the subject, you say so.

A I don't.

Q Now, sir, each time that you executed a loan application, do you recall either in a written form or orally being advised that you should tell the truth in filling out the questionnaire?

A Yes.

Q And notwithstanding that, each time you made out one of these forms, you didn't state the truth, did you?

A Correct.

Q Correct, you did not?

A Yes.

Q Had you ever borrowed money previously from a lending institution?

A No sir.

Q At that time, did you and your wife maintain any bank accounts?

A We had a savings account.

Q Do you know what was in that savings account at that time?

A No.

Q Do you have any idea of the approximate amount of money?

A No.

Q Did you also have a checking account?

A Sir, my wife handled the banking business in the house. I would just ask her. I don't really know.

Q Sir, is this your signature appearing on the comaker's loan form of exhibit 38?

A Right here (indicating)?

Q Yes.

A Yes, that is.

Q I point to the center of the page, First National City and Lincoln appear, is that your handwriting?

A Yes.

Q Did you advise the bank or the lending institution that you had two accounts, one at First National City Bank and one at Lincoln?

A Yes.

Q At least at that time you knew that you had a checking account, isn't that correct?

MR. GARMANSKY: Objection, your Honor. The accounts have not been established what they are. Ask him if one of the accounts was a checking account.

A Yes.

Q Was one of the accounts a checking account, sir?

A Yes.

Q Did you have to ask your wife when you filled out that form whether you had a checking account?

A Yes.

Q You did ask your wife?

A Yes.

Q You remember that?

A Yes.

Q What did you say to her and what did she say to you?

A (No response.)

THE COURT: If you recall.

A Word for word, I cannot.

THE COURT: You had a conversation about it?

THE WITNESS: When we filled out a form there is always a space where you have to fill out if you have a savings account. She had all the information. She told me and I wrote it down.

THE COURT: As to the checking account and the

savings account?

THE WITNESS: Yes.

Q Have you ever had any arguments with Mr. Shevack?

A No sir.

Q Did you ever have any arguments with Mr. Shevack about your estranged wife?

MR. GARMANSKY: Objection.

MR. GOIDEL: I am cross-examining. If every time I hit a jugular vein they start jumping up and arguing --

MR. GARMANSKY: He said he did not have any argument.

MR. GOIDEL: I am trying to refresh his recollection.

MR. GARMANSKY: May we have the question? He said no. He did not have any fights with Mr. Shevack.

THE COURT: He is pressing for an answer. As I say, you must bear in mind that cross-examination isn't polite, and it doesn't have to be polite, and it's purpose is to test credibility. I don't know where this is going but I just can't turn it off.

MR. GOIDEL: Read the question.

(Whereupon the question was read by the reporter.)

A No.

Q Did you ever have any conversations with him about her?

A No.

Q Sir, I believe you stated that you never made any money while associated with Galaxy, is that correct?

A Yes sir.

Q Did you try to make money?

A Yes sir.

Q Did you bring people to opportunity meetings?

A Yes sir.

Q How many people did you bring to opportunity meetings?

A Two or three.

Q Did you ever try to sell food?

A No sir.

Q Now, sir, when you signed the contract, were you cognizant of the nature of the operation of Galaxy?

A Yes sir.

Q When you executed the contract you understood there were two ways to make money, is that correct?

A Yes sir.

Q And that you would have to work in order to earn that money?

A Yes sir.

Q And that you would receive no reward simply by sitting back and not working?

A Yes sir.

Q Do you still own the franchise?

A Yes sir.

Q Did you ever attempt to sell it back to Galaxy?

A Yes sir.

Q When did you attempt to sell it back?

A Well, let's see. After I found out that I wasn't going to be able to make any money in Galaxy.

Q When was that?

A That was the latter part of November 1972.

Q Tell me what facts came to your attention indicating to you you would be unable to earn money?

A I went to the warehouse to find out when I would be able to go about making money in Galaxy. I was told by Mr. Mark Glasser the company wasn't going to be going on a retail operation, it was going to go on a pilot program and I wouldn't be able to make money selling food until March the following year, '73.

Q Is that what you mean having learned you could not earn money?

A Yes.

Q Sir, you don't know whether this is or is not -- can you tell me if this page which is part of plaintiff's exhibit 40 is in your handwriting?

A This page?

MR. GARMANSKY: Can you identify the page?

Q Plaintiff's exhibit 40.

A No sir.

Q This BN 13 on top of it?

A No.

Q Do you know when Mr. Shevack left the organization?

A Not exactly, no. I don't.

Q Do you know if he left the organization before November of 1972?

A He wasin the operation then. I know hewas still in there.

Q When is the last time you recall seeing him?

A Well, I had met him in 1973 when I was working on Wall Street. I happened to have bumped into him on the street with his associate Peter.

Q Did Mr. Shevack go into any of the lending institutions with you and your wife?

A No sir.

Q But it is your testimony that he drove you to

each one of those?

A Yes.

Q At any time, sir, did you go to any of these lending institutions and confess the fact you had done wrong by giving them false information?

A No sir.

Q At any time after having done that did you consult with an attorney?

A No.

Q You say you called the Securities and Exchange Commission, is that correct?

A Yes sir.

Q By the way, this little piece of paper thatyou have in front of you, exhibit 37 --

A Exhibit 37?

Q Who kept that?

A My wife.

Q Was she with ycu when you went to the Securities and Exchange Commission?

A No sir.

Q When did you first see this document after the time that you say you saw it in the car?

A When was the next time I saw it after that period?

Q Yes.

A To my recollection, right now.

Q Do you know who physically handed it to the Securities and Exchange Commission?

A No.

(Continued on next page.)

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Q Had you known anyone that ever worked there?

Q You did not?

A That is correct.

Q How about the W-2 form?

A The same answer, no.

Q In other words, you never saw that W-2 form between the time that you received it in the automobile, and the time that it was shown to you here today?

A My wife had possession of this and the W-2 form.

Q Yes. But my question is, you didn't see it?

A No.

Q But you did know that it is the same form that you had see two years earlier?

A Yes.

Q Now, sir, you testified to certain numbers that were referred to at the Opportunity Meeting. Could you repeat those numbers for us?

A $60,000 a year was on the blackboard, circled.

Q Any other numbers?

A There were at least 50 to 75 people present at the meetings, that I can tell you just by looking at a small crowd.

Q Perhaps you didn't understand me. Were there any other numbers written on the blackboard besides the $60,000 that was circled?

A Yes. It was drawn out, coming to a conclusion

that you could make $60,000.

Q For what?

A If you get a certain amount of customers, and you make a certain amount of commission, and you keep working at it for a period of time, you can make $60,000.

Q If you fulfill the other requirements for earning that $60,000, namely, getting so many customers, and buying so much food, isn't that correct?

A Yes, sir.

Q As a matter of fact, the examples that they gave you referred to earning as little as $125, isn't that so?

MR. LERNER: A year, or a week?

Q (continuing) A week.

A A week, yes.

MR. GOIDEL: I have no further questions of this witness, your Honor.

THE COURT: All right.

Now, what do we want to do?

MR. GOIDEL: May I simply request, however, your Honor, because we may want to recall him at a later time, may we have his business address where he may be reached?

THE COURT: I thought it was stated on the record--

THE WITNESS: Yes.

MR. GARMANSKY: I have it, and I will be happy to

supply it.

THE COURT: Do I understand your wife is here?

THE WITNESS: Yes, she has been sitting out there.

THE COURT: What are we going to do? It is so late, and we have a very aggravated Reporter problem around here.

MR. LERNER: She is to be the last witness. We certainly would want to put her on tomorrow.

THE COURT: Would she be able to come?

THE WITNESS: Excuse me --

MR. LERNER: Maybe we can bring her in and ask her. But that is our case.

THE COURT: This will be the last witness. You are not going to call Mr. Shevack?

MR. LERNER: No.

MR. GOIDEL: May I make a request? May I be permitted to have these Exhibits overnight so I may study them?

THE COURT: Is there any reason why that can't be done? I assume Mr. Goidel is a member of the Bar and understands what his responsibilities are.

MR. LERNER: Possibly I could make copies of the documents.

THE COURT: You don't have any copies?

MR. LERNER: Are these the only copies of the documents, the application forms (addressing Mr. Garmansky)?

MR. GARMANSKY: Yes.

MR. LERNER: I will make copies. And we will be glad to make copies available for Mr. Goidel tonight.

THE COURT: You want to go back to your office?

(Thereupon ensued discussion between counsel out of the hearing of the Reporter.)

MR. LERNER: Do you have any redirect?

MR. GARMANSKY: No.

MS. MYSLIWIEC: Do you think it would take an hour to examine Mrs. Silverman?

MR. LERNER: Oh, I think so.

THE COURT: We will make it 10:00 sharp, sharp, sharp.

MR. GARMANSKY: 10:00 o'clock.

MR. GOIDEL: Your Honor, I would like to ask the witness one further question, if I may.

THE COURT: You just thought of something?

MR. GOIDEL: Yes.

THE COURT: Will you resume the stand?

S T E V E N S I L V E R M A N , recalled as a witness, having previously been duly Sworn, resumed the stand and testified further as follows:

CROSS EXAMINATION

BY MR. GOIDEL: (continued)

Q Sir, I asked you previously whether you and Mr. Shevack had ever had an argument, and your answer to that question was no. I followed it up by a question as to whether there was ever a discussion or argument involving your wife?

A Correct.

Q Is that correct?

A Yes.

Q You never met me before, is that correct?

A Yes, I did not.

Q Is your wife a nurse, sir?

A Yes, sir.

Q What hospital does she work in?

A Coney Island Hospital, sir.

Q I will ask you once again, sir, Was there any argument between you and Mr. Shevack at any time concerning your wife, as a nurse?

A No, sir.

MR. GOIDEL: No further questions.

Your Honor, we have made arrangements for the photostating of those documents.

THE COURT: All right, we will adjourn until 10:00 o'clock tomorrow.

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(Thereupon, at 5:05 o'clock P.M., an adjournment was taken to Thursday, October 10, 1974, at 10:00 o'clock A.M.)

* * *

I N D E X

Witnesses	Direct	Cross	Voir Dire
Melvin J. McLean	1207	1260	1210
Steven Silverman	1304		

Exhibits

Government's		For Id.	In Evid.
32	Card	1209	1211
33	1-pg Document	1251	1251
34	Document	1258	1258
35	Contract	1315	1316
36	Document	1321	1324
37	Document	1321	1325
38	8-pg Document	1326	
39	10-pg Document	1326	
40	11-pg Document	1326	

Defendant's			
Q	1-pg Document	1209	

UNITED STATES DISTRICT COURT

EASTERN DISTRICT OF NEW YORK

----------x

SECURITIES EXCHANGE COMMISSION, :

Plaintiff, : 73-C-1742

-against- :

GALAXY FOODS, et al., :

Defendants. :

----------x

United States Courthouse
Brooklyn, New York

October 10, 1974
10:15 o'clock A.M.

B e fo r e:

HONORABLE EDWARD R. NEAHER, U.S.D.J.

BURTON SULZER
OFFICIAL COURT REPORTER

Appearances:

ALLAN LERNER, ESQ.
HARRY GARMANSKY, ESQ.
REGINA MYSLIWIEC, ESQ.
JULIA WILLIAMS, ESQ.
Attorneys for SEC

ALVIN GOIDEL, ESQ.
Attorney for Defendants Sheback and Kirschenblatt

GEORGE PADILLA
Pro Se

MP:jm
lamR1

THE COURT: Are you ready?

MR. GARMANSKY: The Commission would like to call Mrs. Silverman to the stand.

THE COURT: All right.

G E O R G E T T E S I L V E R M A N , called as a witness, having first been duly sworn by the Clerk of the Court, took the witness stand and testified as follows:

DIRECT EXAMINATION

BY MR. GARMANSKY:

Q Would you state your home address?

A 2135 West 7th Street in Brooklyn.

Q Where are you employed?

A Coney Island Hospital.

Q What do you do there?

A I am a registered nurse.

Q Your husband is Mr. Steven Silverman?

A Yes.

Q Mrs. Silverman, have you ever heard of a company called Galaxy Foods, Inc.?

A Yes.

Q When, for the first time?

A October, '72.

Q Would you please tell the Court the circumstances under which you heard of the company?

A I had a friend at school and she had told me that

her boyfriend was in the company and doing very well and I had been interested in making some extra money and told us we should get together.

Q Did you communicate this to anyone?

A My husband.

Q Did you ever attend any Galaxy meetings?

A Yes.

Q When, for the first time?

A October, early October, '72.

Q How did you get to the meeting?

A Arthur Shevack, his wife, and his friend Peter and myself drove in the car.

Q Who else was in the car with you besides those people?

A Arthur Shevack, Peter, Arthur Shevack's wife, myself, and my husband.

Q Was there any discussion concerning Galaxy on the way to the meeting?

A Very little. We asked questions about the company.

Q Who is we?

A My husband and myself. And Mr. Shevack said that we should wait until we got to the meeting. We should wait until we got to the meeting to see what it was all about.

And if we had any questions afterwards, he would answer any questions.

Q Was this the first time you met Mr. Shevack?

A Yes.

Q Now, Mrs. Silverman, who introduced you to Mr. Shevack?

A Mr. Shevack himself when we first met. He came and picked us up.

Q Who set up the appointment that Mr. Shevack would pick you up?

A We got a phone call from him and he told us he would be there to pick us up.

Q Did you and your husband subsequently decide to invest in Galaxy?

A Yes.

Q How much did you invest?

A Seven thousand dollars.

Q How many more meetings did you go to before you decided to invest?

A We went to the first meeting and I think -- I think that was it. After we went to the first meeting we decided.

Q Did you have the necessary funds to invest in Galaxy?

A No.

Q How did you get the money to invest in Galaxy?

A Mr. Shevack assisted us in getting loans from banks and loan companies.

Q Mrs. Silverman, I would like to show you what has been marked in evidence as Plaintiff's Exhibit 36, do you recognize it?

A Yes, I do.

Q When, for the first time, did you see Plaintiff's Exhibit 36?

A When Mr. Shevack had taken us to get loans.

Q When was this?

A In October of '72.

Q Who gave you Plaintiff's Exhibit 36?

A Mr. Shevack.

Q Please tell us the circumstances surrounding Mr. Shevack giving you Plaintiff's Exhibit 36?

A Well, we had to fill out applications for loan companies and in order to get the loans I needed a job and at the time I was in school. And Mr. Shevack said he would take care of it and give me something to show that I was working and he gave us the W-2 form and said I should use it.

Q Who told you you had to have a job if you went to a bank?

A Mr. Shevack.

Q Did you tell Mr. Shevack you were not working?

A Yes.

Q Did you aid or assist in any way in the preparation of Plaintiff's Exhibit 36?

A No.

Q Now, Mrs. Silverman, does your name appear on Plaintiff's Exhibit 36?

A Yes, it does.

Q Is there a social security number appearing next to your name?

A Yes.

Q Is that your number?

A Yes.

Q Did you at any time give Mr. Shevack your social security number?

A Not that I remember.

Q Now, the name on Plaintiff's Exhibit 36 is A&M Dental Labs as the place of employment. Prior to your seeing Plaintiff's Exhibit 36 in October of '72, had you ever heard of that company?

A No.

Q Had you ever worked there?

A No.

Q Had you known anyone that ever worked there?

A No.

Q I would like to show you what has been marked in evidence as Plaintiff's Exhibit 37, do you recognize it?

A Yes, I do.

Q When, for the first time, did you see Plaintiff's Exhibit 37?

A The same time I was handed the W-2 forms. When we were going to make the loan application.

Q Who gave you Plaintiff's Exhibit 36?

A Mr. Shevack.

Q Strike that, Plaintiff's Exhibit 37.

Mr. Shevack?

A Yes.

Q Where did Mr. Shevack give you Plaintiff's Exhibit 37 and the other document I just showed you, Plaintiff's Exhibit 36?

A In his car.

Q I see. Now, Mrs. Silverman, whose handwriting appears on Plaintiff's Exhibit 37?

MR. GOIDEL: Objection.

MR. GARMANSKY: If the witness knows, she may answer.

MR. GOIDEL: I don't think that is proper. You

can ask if she saw it being written --

THE COURT: You can ask her if she saw it being written, do that first.

BY MR. GARMANSKY:

Q Mrs. Silverman, did you see Plaintiff's Exhibit 37 being written at or about the time Mr. Shevack gave it to you?

A Yes.

Q Who wrote Plaintiff's Exhibit 37?

A Mr. Shevack.

Q Does anyone else's handwriting appear on Plaintiff's Exhibit 37, besides Mr. Shevack's?

A Yes, mine.

Q Can you tell us what you wrote on Plaintiff's Exhibit 37?

A Immediate supervisor, Francis Alexander.

THE COURT: You wrote that?

THE WITNESS: Yes. And one hundred and sixty-five dollars.

BY MR. GARMANSKY:

Q The rest of the handwriting you saw Mr. Shevack fill in?

A Yes.

Q Did anyone instruct you to write immediate

supervisor Francis Alexander and one hundred and sixty-five dollars?

A Yes, Mr. Shevack.

Q What did he say to you?

A He said I may need the additional information on the loan application so he gave me the name and the amount of money I made per week.

Q You testified that Mr. Shevack gave you Plaintiff's Exhibit 36, the W-2 statement, and Plaintiff's Exhibit 37, while you were in his car, is that correct?

A Yes.

Q Where were you sitting in the car when Mr. Shevack gave this to you?

A I believe it was in the back seat of the car.

Q Who was sitting with you in the back seat?

A My husband.

Q Now, Mrs. Silverman, approximately how many banks or lending institutions did you go to with Mr. Shevack?

A Approximately six.

Q Do you recall any of the names?

A Yes.

Q Please tell us.

A First National City Bank, Manufacturers Hanover Trust, two loan companies, Household Finance and Family Finance.

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And two other banks I can't remember the names of.

(continued on next page)

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DIRECT EXAMINATION

BY MR. GARMANSKY (Cont'd):

Q Now, did Mr. Shevack, prior to going to any of these banks and finance companies, give you any instructions concerning the loan applications?

A Yes.

Q Tell us what he said to you.

A Before going into the first bank, he had a loan application with him, and he told us we should fill in it's for furniture, not for joining Galaxy Goods. I should use the information on the W-2 form and the little piece of paper as far as my job goes.

Q Now, did you say anything to Mr. Shevack at that time?

A Well, I knew it wasn't true. I felt uneasy about it. He said, "You don't have to worry about it. We've used this before and it will work."

Q Did you fill out the loan applications at banks and finance companies?

A Yes.

Q Did anyone accompany you in to banks?

A My husband.

Q Did you and he fill out the applications together?

A Yes.

Q I would like to show you what has been marked in evidence as Plaintiff's Exhibit 38. Do you recognize this?

A Yes, I do.

Q Would you please tell the Court what Plaintiff's Exhibit 38 is?

A An application to Manufacturers Hanover Trust for a loan.

Q Is this the copy of the application you made with your husband in October, 1972?

A Yes.

Q Does your signature appear on this loan application?

A Yes, it does.

Q Reading from co-maker's statement, now, did you put down A & M Dental Lab as your place of employment on the application, Plaintiff's Exhibit 38?

A Yes.

Q I would like to show you what has been received in evidence as Plaintiff's Exhibit 39. Do you recognize it?

A I recognize part of it.

Q Is this one of the loan applications that you and your husband filled out that day?

A He didn't fill this out.

Q Not this particular page, but this.

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A We signed this, yes. Is this Family Finance?

Q Yes, Family Finance Corporation.

A This was the loan that we had nothing to do with really except to go in and sign for it and show proof we were working.

Q You just signed this loan with your husband?

A Yes.

THE COURT: You said, "And show proof."

THE WITNESS: We had to show the W-2 form and my husband's W-2 form.

Q That is Plaintiff's Exhibit 36?

A Right.

Q I would like to show you what has been received in evidence as Plaintiff's Exhibit 40; do you recognize this?

A Yes, I do.

Q Was this one of the applications you and your husband filled out?

A Yes.

Q Did you sign this application?

A Yes.

Q Mrs. Silverman, did you receive any loan proceeds from these applications?

A Yes.

Q How much did you and your husband receive?

A Approximately $6,000.

Q You testified that the investment in Galaxy cost you $7,000; is that correct?

A Yes.

Q Where did you get the other $1,000?

A We had some money in our savings account, maybe $600, and the rest of it Mr. Shevack supplied us with and said as soon as we started making money in the company, we could pay him back.

Q Mrs. Silverman, didyou go to all these banks with your husband,and finance companies, in one day?

A No.

Q How long a period of time did you go to these banks and finance companies?

A We went into all of them except on the first day. I can't recall wnther it was the next day or day after that. Then we had to go to Family Finance because we didn't receive all the monies we applied for.

Q Did Mr. Shevack take you to Family Finance?

A Yes.

Q Mrs. Silverman, did Mr. Shevack give you any instructions concerning what to put on the loan applications about outstanding debts?

A Yes. He told us not to put -- if we had been

in one bank prior to that, not to put down any other loans.

Q Did he give you any reason for this?

A We wouldn't get the loan.

Q I would like to show you Plaintiff's Exhibit 37, Family Finance Corporation, it has on the next to last page a list of previous debts and has Household Finance, $1,878; is this your handwriting?

A No, my husband's.

THE COURT: Did you refer to that as Plaintiff's Exhibit 37?

MR. GARMANSKY: 39.

Q Did you know that your husband was going to list Household Finance as a debt on the Family Finance application?

A Yes, I did.

Q Could you please tell us why you and your husband listed that, contrary to Mr. Shevack's instructions?

A As I said previously, we did not go to Family Finance until maybe a day or so after we applied to other companies, and somehow they had found out about the Household Finance loan, so Mr. Shevack told us we have to put it down.

Q When you went to Family Finance, did Family Finance tell you "We know about the loan at Household Finance"?

A We didn't discuss anything.

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Q Mr. Shevack just told you before going to Family Fanance to put down you received money from household Finance?

A Yes.

Q In other words, you did follow Mr. Shevack's instructions?

A Yes.

Q Do you recall coming to the Securities and Exchange Commission to talk about what you just testified to today?

A Yes.

Q Do you recall anyone at the SEC saying anything to you about these bank notes?

A Yes.

Q Do you recall what anyone said to you? Do you recall who said it and what was said?

A We talked with you and you just told us that, you know -- we discussed how we had gotten the loans.

Q Do you know whether or not anyone at the SEC told you what you did with these banks could be an illegal act?

A Yes.

Q In exchange for your testimony here today, did the SEC give you any promises whatsoever?

A No.

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7 MR. GARMANSKY: I have no further questions, your honor.

MR. GOIDEL: Your honor, Mr. Garmansky's direct testimony was quite fast. I would like one minute to call my office to have my witness appear here.

THE COURT: All right.

MR. GOIDEL: We don't need an adjournment. I will just make the call.

THE COURT: All right.

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(Continued on next page.)

CROSS-EXAMINATION

BY MR. GOIDEL:

Q Mrs. Silverman, please tell us your Social Security number.

A 063,38,0248.

Q Now, you testified on direct examination by Mr. Garmansky, that you did not provide Mr. Shevack with that number, is that correct?

A I said I don't recall providing him with that number.

Q Is there any doubt in your mind?

A No, I just don't remember.

Q Let us analyze that. You spoke with Mr. Shevack for the first time on the telephone, is that correct?

A Yes.

Q You say Mr. Shevack called you, is that correct, or did you call Mr. Shevack?

A He called us.

Q Who had given Mr. Shevack your telephone number?

A I believe it was the girl from the school.

Q Do you know that to be a fact?

A Yes.

Q Did he call you during the day or in the

evening?

A In the evening.

Q Do you recall what month it was?

A In October '72.

Q Do you recall what day?

A No.

Q How long was that telephone conversation?

A Not more than five or ten minutes.

Q Did you give Mr. Shevack your Social Security number at that time?

A No.

Q Now, when after that telephone conversation did you first physically meet Mr. Shevack?

A I believe it was the next day.

Q In between, were there any other telephonic communications between you?

A No.

Q The next day is when you went to the Opportunity Meeting, is that correct?

A Yes.

Q And you testified as to who was present in the automobile, including Mr. Shevack, Mrs. Shevack, Peter, yourself and your husband?

A Yes.

Q During that ride, did you give Mr. Shevack or anyone else your Social Security number?

A No.

Q You arrived at the meeting, you listenend to what was said there?

A Yes.

Q Did you thereafter speak with Mr. Shevack while at that meeting?

A Yes.

Q Do you recall giving him your Social Security number?

A No.

Q When is the next time that you had occasion to speak with Mr. Shevack?

A We spoke to him after the meeting and then we spoke to him the next day when we went for the loans.

Q That was the very next day you started to secure loans to make a purchase?

A Yes.

Q It was during that ride that Mr. Shevack handed to you this W2 Form which is marked as Plaintiff's Exhibit 36, is that correct?

A Yes.

Q And it had your Social Security number on it?

A Yes.

Q Let me ask you this; did you give anyone else your Social Security number?

A No.

Q You do have a card on which your Social Security number appears?

A Yes.

Q Is that correct?

A Yes.

Q Did you ever find that card as missing from your pocketbook?

A No.

Q Did you ever show it to anyone?

A Not that I remember.

Q By the way, where did you live at that time?

A 2327 West 13th Street in Brooklyn.

Q Did you ever hear of A&M Dental Laboratories?

MR. GARMANSKY: A&M Dental Laboratories.

A Not prior to Mr. Shevack telling me about it.

Q You are a nurse?

A Yes.

Q You were attending nursing college or school at the time?

A Yes, Kingsbrook Community college.

Q Do you know whether A&M Dental Laboratory does any work for the hospital you are associated with?

A No, I do not.

Q Do you know the address of A&M Dental Laboratories?

A No.

Q Do you know whether it's located in Brooklyn?

A Yes, I do.

Q Do you know where in Brookly?

A No, not offhand.

Q If I mention to you Ocean Avenue, would that refresh your recollection?

A No.

Q Did you ever have occasion to travel on Ocean Avenue?

A Yes.

Q You ever have occasion to see a sign in front of any building that said A&M Dental Laboratory?

A No.

Q Now, there is an employer's identifying number on the W2 Form as well. Did you ever see that employer's identification number before?

A Not before I was handed the W2 Form by Mr. Shevack.

Q Now, do you have any explanation for us at all, as to how Mr. Shevack is purporting to have obtained your Social Security number?

A No.

MR. GARMANSKY: Objection, your Honor.

MR. GOIDEL: If she has any facts, that is all.

THE COURT: I will overrule the objection.

You may answer.

A No, I don't.

Q Did Mr. Shevack ever go into any of the lending institutions with you?

A No.

Q Let us take these lending institutions one at a time if we can, do you recall the first lending institution to which you went?

A I don't recall the name, I recall approximately where it is located.

Q Was it in Brooklyn?

A Yes.

Q And it was before leaving the vehicle that you drove there in, that Plaintiff's Exhibit 36, that is the W2 Form, and Plaintiff's Exhibit 37, this little sheet of paper, were handed to you, is that correct?

A Yes.

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Q Who drove?

A Who drove?

A Yes.

A Mr. Shevack.

Q When did Mr. Shevack, in your presence, write that piece of paper?

A After we had parked in the front of the bank.

Q What bank?

A As I said before, I don't remember the name of the bank. It was located on 86th Street in Brooklyn.

Q Are you aware that your husband has testified that that was handed to you while Mr. Shevack was driving?

MR. LERNER: Objection.

MR. GARMANSKY: Objection, your Honor.

MR. GOIDEL: Fine. I will read --

MR. LERNER: Misleading.

Q I will read you questions and answers and you tell me at the end whether the statements contained are accurate or inaccurate.

"Question: Did he hand that --"

MR. LERNER: Excuse me. Where is that?

MR. GOIDEL: I'm sorry. I'm reading from page 1355 of the transcript.

MR. LERNER: Thank you.

Q "Question: Did he hand that to you while he was driving?

"Answer: I believe. Well, when he handed me the W-2 form, he handed me this statement.

"Question: Was he driving at the time?

"Answer: Was he driving?

"Question: Yes.

"Answer: When we had gotten to the bank.

"Question: When you had gotten to which of the banks?

"Answer: It had to be the first one, because when I went into each bank, I presented the W-2 form.

"Question: Did he hand it to you while in the car?

"Answer: Yes, he must have. Yes."

Are those statements all correct?

A Yes.

Q Okay. I apologize because I had misread it. Okay.

Now I'm asking you again, was he in the car or outside of the car?

A He was in the car.

Q In the car.

Was he still behind the driver's wheel?

A I believe so.

Q Okay.

And he wrote it while sitting there behind the driver's wheel?

A Yes.

Q Then he handed it to you?

A Yes.

Q And then he said to you, by the way, or words of that substance, you need more facts; is that right?

A He said I may need some more information for the loans.

Q Okay.

Did you have a pen?

A Yes, I did.

Q You opened up your pocketbook and took it out?

A Yes, I did.

Q Then you wrote it down?

A Yes. No.

Q You didn't hand it back to him to fill in the information?

A Excuse me .

Q Yes?

A He gave me the information that was on the paper, A and M Dental Labs and the address.

Q Yes.

A He handed me the paper and then he said, "You may need extra information."

Q How much -- I'm sorry, go ahead.

A So then he gave me the immediate supervisor's name and the amount of money that I made per week.

Q But the important thing is that he physically wrote this while in your presence, seated behind the wheel of the car?

A Yes, he did.

Q Okay.

How much time transpired between the time of his handing this paper to you and the time that he told you that you might need additional facts?

A Maybe a few minutes.

Q Well, did you have any discussion while in the automobile about anything else after he handed this to you and after you had parked the car?

A He just reminded us about filling out the application, that it was for furniture and that I should use this information.

Q Okay. So then you went into the bank with this information?

A Yes.

Q And did you put it down on the table while filling out the application?

A Well, there are -- there are tables in the bank. Not at the desk of the bank representative.

Q I'm asking you, did you put this down on the table?

A Yes. Yes, we did.

Q Okay.

Then you submitted the loan application right then?

A Yes.

Q Fine.

Is this the routine you followed on each occasion that you went to one of the lending institutions?

A Yes.

Q In other words, you'd go in, fill out the application? After completing it, hand it in?

A Yes, except for one.

Q Fine. Which one?

A Family Finance.

Q Okay.

What happened at Family Finance that differed from any of the other trips that you made?

A Family Finance was applied for a different

day and Mr. Shevack had found out that we did not receive all the money that we had applied for in the first day, so --

Q When you say "on the first day" you mean from other institutions?

A Yes.

Q Okay. Go ahead.

A So he had called up Family Finance himself and had told them, you know, had given them the information that we had, Steven's information, my husband's information, and the information about A&M Dental Labs, my employment, and then he took us there and we filled -- we just signed the application. We didn't even fill out anything because they already had it all filled out for us.

MR. GOIDEL: Sir, will you please read back that last answer?

(Record read.)

(continued next page.)

CROSS-EXAMINATION

BY MR. GOIDEL (Cont'd):

Q I'm showing you a form which is part of Plaintiff's Exhibit 39. I ask you if you can identify the handwriting on that form?

A Yes. That's my husband's.

Q When did he complete that?

A It was done at the same time that we went in for the application.

Q Now, when you were there, you learned that they had come aware of the Household Financie information?

A Not while we were there. We learned that before we went into the office.

Q I see. So then you completed this?

A Yes.

Q And you listed the Household Finance?

A Yes.

Q Had you already received the check from Household Finance?

A I believe we did.

Q So that you knew the exact amount?

A Yes.

Q They didn't tell you over at Family Finance that they knew about it?

A We didn't discuss that.

Q You didn't?

A Mr. Shevack was told that over the phone.

Q I understand. Were you present when Mr. Shevack made that call?

A No, I was not.

Q Now, what day of the week was it that you started going around for these loans, if you know?

A I can't remember.

Q How many days in all did you go around making these loans?

A Just two days.

Q Did you have school those days?

A Yes, I did.

Q Did you cut school?

A Yes, I did.

Q Did your husband cut work?

A Yes, he did.

Q You didn't select times that were conducive to your attending both your classes and your going for loans?

A No, we didn't.

Q Now, when you went for these loans, was anyone other than your husband and you and Mr. Shevack present?

A Mr. Cancilla.

Q Were both of them present?

A Yes.

Q Did Mr. Cancilla perhaps hand you this paper?

A No, he did not.

Q It was Mr. Shevack?

A Yes, it was.

Q And it was Mr. Shevack who was also driving the vehicle?

A Yes, he was.

Q Did you ever go back to the bank or the lending institutions and advise them of the fact that you had given them improper information?

A No, we did not.

Q Or failed to provide them with adequate information on the basis of actual facts?

A No.

Q Did you ever consult with anyone to ascertain whether you should do so?

A No.

Q Did you and your husband ever discuss it?

A About going back to them and telling them? No.

Q You just let it rest even though you knew it was wrong?

A Yes.

Q Had you ever borrowed money previously?

A No, we had not.

Q You said that you had some savings; is that true?

A Yes.

Q What bank?

A Lincoln Savings Bank.

Q Did you try to go to the Lincoln Savings Bank to make a loan?

A No, we did not.

Q What was your balance on deposit at that time at the Lincoln Savings Bank?

A Approximately $600.

Q Do you recall ever telling Mr. Shevack that you had a savings account in the Lincoln Savings Bank?

A Yes.

Q When did you tell him this? I mean, specifically that you had it in that bank.

A After we had found out that we still needed more funds and he drove us to the bank to withdraw the money that we needed to help pay for the franchise.

Q In other words, you first notified him of the existence of an account in that particular bank following your attempt to obtain all the funds through loans?

A Yes.

Q Now, you also had an account, a checking account; is that correct?

A Yes.

Q Did you ever notify Mr. Shevack of the particular bank in which you had your checking account?

A I believe when we drove up to that bank to apply for a loan, I toldhim we had a checking account there.

Q I see.

A We didn't go to the branch that I had the checking account at but we went to one of the branches.

Q I see. It was coincidence that you happened to to first to a bank wherein you already maintained an account; is that what you are saying? First National City Bank, that is?

A We didn't go there -- I don't understand what you are saying.

Q Did you go to the First National first?

A It wasn't the first bank we went to.

Q Where did you go first, if you know?

A I already told you --

MR. LERNER: Asked and answered.

Q Is that the bank, the name of which you don't recall?

A Yes.

Q Did you get a loan at that first one, the name of which you do not recall?

A No.

Q Was First National City Bank the second Band to which you went?

A No.

Q Did you go to a Branch of First National City Bank in Brooklyn?

A Yes, we did.

Q But not the one where you had your account?

A No.

Q Where was that bank?

A The bank is located in the Korvette Shopping Center, in Brooklyn, Bay Parkway.

MR. GARMANSKY: Your Honor, may we have a clarification here? Which bank was it, the one they had a checking account or the one they went to for the loan?

MR. GOIDEL: She just said that they are not the same. That's --

MR. GARMANSKY: I know but which bank is she identifying.

THE WITNESS: This is the bank that we went to for the loan.

Q Where is that in relation to your home?

A Approximately a mile, a mile and a half away.

Q How much money in all did you borrow?

A Approximately $6,000.

Q How much money did you actually realize; in other words, how much was actually given to you out of the $6,000 by the banks and institutions?

THE COURT: Do you understand the question?

THE WITNESS: I understand but --

Q In other words --

A I'm saying, the -- we had approximately $6,000 to give for the company. That's what.

THE COURT: That was the net? That was the net?

THE WITNESS: Yes.

Q And in all, how many loans did you actually make?

A Four.

THE COURT: How much was the gross total of the loans?

THE WITNESS: I coulun't tell you offhand.

Q When was the first time that you ever heard anything about borrowing money for an investment in Galaxy?

A In -- the night that we had decided that we wanted to join Galaxy.

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Q That was at the Opportunity Meeting or after?

A After the Opportunity Meeting.

Q And where was that discussed?

A I'm not quite sure where it was discussed. It may have been discussed on the way out to the car. It may have been discussed in the car.

Q Was it ever mentioned at the Opportunity Meeting itself?

A I'm not sure.

Q Can you tell us what was discussed at the Opportunity Meeting?

A We thought that it was a great idea and that we'd like to join. But that we just didn't have the funds.

Q No. Tell me, what was discussed at the Opportunity Meeting?

A At the Opportunity Meeting?

Q Yes.

MR. GARMANSKY: Can we have by who?

Q Were there speakers at the Opportunity Meeting?

A Yes, there were.

Q Would you tell us what the speaker said and if you can identify the individual speaker, would you do so?

A I can only remember two names of speakers. One was Steve Roth and one was George Padilla.

THE COURT: George --

THE WITNESS: Padilla. They -- they summarized the operations of the company. They would put -- they had a blackboard and they would give us figures of how many customers you could -- could bring how much money.

BY MR. GOIDEL:

Q In other words, they told you that if you brought so many customers and sold so much food, that you could obtain so much commission from the sale of that food?

A That's right.

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CROSS-EXAMINATION

BY MR. GOIDEL: (Cont.)

Q Is that correct?

A Yes.

Q And do you remember any specific figures that were used?

A I believe you could make about $60,000 a year. Something like that.

Q Fine. And did they show you how you could earn that 60,000?

A Yes, they did.

Q Were you aware of the fact that you could earn less than 60,000?

A It all depended on how many customers you got so if you didn't get as many as they showed you on the blackboard, you would make less.

Q And that you understood?

A Yes.

Q Did Mr. Shevack ever say other than that to you?

A I don't understand what you are trying to say.

Q Mr. Shevack ever guarantee you that you would earn $60,000?

A No, he didn't.

Q You understood the facts from the presentation at the meeting?

A Yes, we did.

Q Do you remember the name of the friend that put you in contact with Mr. Shevack?

A Yes.

Q Or put Mr. Shevack in contact with you?

A Yes, I do.

Q What is the name?

A Teresa Varano.

THE COURT: Teresa?

THE WITNESS: Varano, v-a-r-a-n-o.

THE COURT: Varano.

THE WITNESS: Varano.

THE COURT: "V"?

THE WITNESS: "V".

BY MR. GOIDEL:

Q When did you and your husband separate?

A It will be a year in --

MR. LERNER: Your Honor, I don't think there has been any testimony that they have separated.

MR. GOIDEL: Mr. Silverman mentioned it in yesterday's testimony.

THE COURT: Well, he did, that's true.

MR. LERNER: Then,your Honor, I'd like to make --

THE COURT: Let me ask you this: What relevancy would that have?

MR. GOIDEL: Hostility.

THE COURT: Hostility to whom?

MR. GOIDEL: Hostility to Mr. Shevack.

MR.LERNER: Your Honor, can we have an offer, please, at a side bar? Rather than getting this on the record.

(Side bar discussion follows.)

MR. GOIDEL: It is difficult to speak with her staying over there. There was an incident that took place. I think it was in around October of last year.

Mr. Shevack will be here to testify to it. Where Mr. Silverman accused Mr. Shevack's brother of having a relationship with his wife. Not Mr. Shevack, personally, but Mr. Shevack's brother. And blamed Mr. Shevack for not interceding between him and his wife.

If you wish that I preserve this line of questioning until Mr. Shevack does actually testify

with regard to it, fine. That, for example, your Honor, is exactly why I said, "Did you ever"-- yesterday in my question, "Did you ever meet me before? Is your wife a nurse?"

We had no reason to know prior to that time that he would be called or she would be called to testify in this action.

THE COURT: Except that when you describe might tend to show some hostility on the part of her husband but not necessarily on her part.

MR. GOIDEL: Well, if I would have to develop it further to show that there is reason for the husband and the wife at this particular moment to be amicable towards each other.

MR. LERNER: He could have asked questions of the husband.

THE COURT: Yes. I would have thought --

MR. GOIDEL: That's one of the reasons why, if you recall, I did so. I might want to call him back to the stand. I didn't want to --

MR. LERNER: I still insist that he call him back and ask the questions of the husband.

MR. GOIDEL: Then I will have to do that.

MR. LERNER: It's the husband's hostility.

MR. GOIDEL: Certainly the wife might know what the reason for this separation is all about.

THE COURT: Well --

MR. LERNER: I would go as far as to allow ---

MR. GOIDEL: It's embarrassing to go into this line of questioning, I grant you, but --

THE COURT: Well, it depends on what the line of questioning is going to be.

The husband has testified they are separated and your question was when.

MR. GOIDEL: My first question was when. You want me to drop it as soon as I learn when?

THE COURT: No. I mean, what I was thinking of was, on this question of hostility to the husband -- of the husband to Shevack, since the husband has already testified here and may be recalled, you might ask if she is aware of any discussions her husband may have had with reference to Shevack with reference to any conduct of hers.

If you want to do it in that general way, you can see what her answer will be. It seems to me again, it's more as -- has more bearing on the husband's attitude and mind than hers.

MR. GOIDEL: Excepting there is testimony, your Honor, which was prepared simultaneously.

I will go into that, if you prefer, first. Communicated with each other, their testimony was rehearsed together. She still hasn't explained the Social Security number.

MR. LERNER: I think she --

THE COURT: That's something else again.

MR. LERNER: That's your opinion.

MR. GOIDEL: That's not my opinion. She --

MR. LERNER; She does not recollect. She may or may not have.

MR. GOIDEL: My attitude is rather damaging. Perhaps she will say she gave it to his brother. I don't know. I think the burden is on her to explain it.

MR. LERNER: You already explored the area.

THE COURT: Well, I will permit you to inquire whether she knows of discussions between her husband and Shevack, whether her husband told her of any discussions he had with Shevack concerning alleged conduct.

MR. GOIDEL: Okay.

(In open court.)

CROSS-EXAMINATION

BY MR. GOIDEL: (Cont.)

Q Mrs. Silverman, are you aware of any discussions had between MR. Shevack and your husband relative to your conduct, of any type?

A No, sir.

Q Your husband never discussed it with you, never discussed any such possible conversation with you?

A NO.

Q May I just have the date of your separation?

A It will be a year ago, November 1st.

Q Have you and your husband discussed how the $7,000 which you invested would be divided between you, if you were to be given $7000 in restitution?

A How it would be divided?

Q Yes.

A Well, as it is now, I am paying only one of the loans. My husband is paying three of the loans. So he would get -- the proportion to what he is paying.

Q Did you two discuss that?

A Yes, we have.

Q Did anybody ever tell you that there was a possibility of your realizing the return of the $7,000?

A No, there was really no -- nobody ever said we'd

get back $7,000.

Q How did the discussion come up as to what would be done with the $7,000, if you did get it back?

A Well, there is always hope that maybe we might get it back and if we did -- or any portion of $7,000.

Q What led you to believe that there was that possibility of getting it back?

A When we had joined the company, I believe there was a clause that if the operations didn't assume within a certain amount of time we would be able to get back the money that we had invested.

Q Mrs. Silverman, you have any understanding or belief that possibly through this litigation, the possibility might exist of your recouping at least all -- a portion if not all of your entire investment?

A No, I don't believe so.

Q You don't believe it?

A I don't believe we'll get back anything, no.

Q Well, did you ever hear the word disgorgement?

A No.

Q Did you ever hear anybody discuss the fact that the defendants in this action were being requested to return funds to the defunct corporation for possible return to those who had purchased franchises?

A I believe it might have been mentioned.

Q When might that have been mentioned to you?

A I really don't remember when. I just remember that I might have heard it. My husband might have mentioned it to me. I don't really know.

Q Give us an approximate time when this came to your attention. A year ago? Six months ago? Three weeks ago?

A I really don't know.

(continued next page.)

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Q When did this discussion take place between you and your husband with regard to how you would divide up the proceeds if it were forthcoming?

A I guess around the time we might have been separated.

Q Had you already gone to the Securities and Exchange Commission as of that time?

A No, I don't think so.

Q When did you go to the Securities and Exchange Commission?

A I don't remember when we first came to the Securities and Exchange Commission.

Q How many times did you go to the Securities and Exchange Commission?

A Maybe two or three times.

Q Did anyone advise you to go to the Securities and Exchange Commission?

A My husband notified me that he was notified by the Securities and Exchange Commission and that I should be here.

Q Did you not go to the Consumer Affairs Department of the City of New York?

A I did not, my husband did.

Q Was it after that visit, too, that your

husband told you that you were going to the Securities and Exchange Commission?

MR. LERNER: Objection, that calls for hearsay.

MR. GOIDEL: Hearsay?

THE COURT: I will allow that if the witness remembers.

A It was after. I don't know how long after.

Q Did you at all, at any time, go to the Consumers Affairs Department?

A No.

Q Did you at any time, commence any action against Mr. Shevack for anything whatsoever?

A No.

Q Did your husband, to your knowledge?

A No.

Q Acting for himself or as your agent, ever commence any lawsuit against Mr. Shevack for fraud or providing you with false information or anything of that sort?

A No.

Q Did you bring any people to any opportunity meetings?

A No .

Q Did your husband?

A Yes.

Q Were you present when your husband brought the people to the opportunity meetings?

A Once.

Q How many times, to your knowledge, did your husband go to opportunity meetings with prospective purchasers of franchises?

A Maybe two or three times.

Q Do you know whether your husband took a sale or took an application for a franchise from anyone?

A No.

Q On the one occasion you were present with your husband, was there a prospective franchisee present?

A Yes.

Q Do you know who that was?

A A relative of my husbands.

Q Do you know his name?

A Howard Silverman.

Q Do you know if Mr. Silverman ever became associated with the corporation?

A He did not.

Q Did there ever come a time when you went to Galaxy Foods and asked Galaxy Foods if they would buy back the franchise?

A My husband wrote a letter to Galaxy Foods stating he had to get out of Galaxy.

Q Did you ever ask them to buy back the franchise you had purchased?

A We asked for our money back.

Q You did, in that letter?

A I believe so, yes.

Q Do you know when that letter was sent?

A Maybe in December or January of -- either December of '72 or January of '73.

Q Was that after or before your husband had gone to the Consumer Affairs Department?

A That was before.

Q Did you provide anyone with a copy of that letter?

A We provided the Securities and Exchange Commission.

MR. GOIDEL: May I ask for the production, if it is here in court?

MR. LERNER: Yes.

(Pause.)

Q In the interim, I will ask you, did you ever ask Mr. Shevack for your money back?

A No.

Q Do you know anyone by the name of Francis Alexander?

A No.

Q Do you know if Francis Alexander is a man or a woman?

A No.

MR. LERNER: Objection. She just said she doesn't know who Francis Alexander is. Now he is asking if it is a man or a woman.

THE COURT: Sustained.

MR. GOIDEL: When you're ready with that.

MR. LERNER: Let the record indicate I am handing over to Mr. Goidel a letter addressed to Mr. Bruce Katz of Galaxy Foods for Mr. Steven Silverman, dated December 29, 1972.

(Pause.)

Q Within the past two years, have you been ill?

A Yes.

Q Will you describe for us the nature of your condition which you were suffering from or are suffering?

MR. LERNER: Objection. I don't see the relevancy of the question.

MR. GOIDEL: Once again, it has to do with

the credibility of the witness.

MR. LERNER: How far afield can you go?

MR. GOIDEL: When you produce a witness who testifies as to certain facts for which there is no explanation as yet, perhaps there are other facts -- well, let me ask:

Q I show you this letter. Did you ever see that letter before, or the original of it?

A Yes.

Q Is that the letter which your husband wrote to Galaxy Foods?

A Yes, it was.

Q Do you know where the original of the letter is?

A No, I don't.

Q But this is an exact copy, a carbon copy?

A Yes.

MR. GOIDEL: I offer this in evidence.

MR. LERNER: No objection.

THE CLERK: So marked as defendant's exhibit R in evidence.

(So marked in evidence.)

Q Are the statements contained in this letter honest, true, accurate?

A Yes.

MR. LERNER: Can the witness see the letter, please?

MR. GOIDEL: Of course.

A They are, yes.

Q Your husband starts this letter by saying, "I have been very pleased to be a part of this organization."

Was that also true?

MR. LERNER: Object. It's hearsay.

MR. GOIDEL: I already established it was written both for her and him.

MR. LERNER: That was not established, your Honor. She testified that her husband requested his money back from the organization.

Q Did you and your husband own this franchise together?

A Yes.

Q There is a statement, "I have been very pleased to be a part of this great organization." Were you aware --

MR. LERNER: Objection, my objection still stands.

MR. GOIDEL: May I finish my question,

please?

MR. LERNER: Forgive me.

Q Were you aware of the appearance of that statement in that letter before it was mailed out?

A I don't remember if I had seen the letter beforehand.

Q When did you first see it?

A Probably after my husband had sent it. I don't remember when I saw it first.

Q Do you have a typewriter at home?

A No.

Q Did you, at that time?

A No.

Q Do you know who typed this?

A My husband's mother.

Q Do you know where your husband's mother typed it?

A I guess her place of employment.

Q Madam, I call your attention -- do you type?

A No, I don't.

Q You never typed?

A No.

Q You don't know the difference between an office or standard typewriter or a portable typewriter?

A No.

Q You would not be able to tell the difference?

A No.

Q You don't recall now seeing this before it was mailed?

A I am not sure if I saw it before it was mailed.

Q Is there anything that would refresh your recollection as to whether or not you did see it before it was mailed?

A I knew of my husband wanting to write a letter to the company because of that situation, but I don't remember seeing it. I am not sure if I saw it before or after. We had this copy so I might have seen it after.

Q At the time that he wrote this letter, were you ill?

A Yes, I was.

Q Were you still attending school?

A Yes.

Q Throughout the period of your illness, were you attending school?

A Yes, I was.

Q Were you seeing any doctors in connection with your illness?

10

Silverman-cross/Goidel

A I wasn't in a hospital, I was in school. There aren't any doctors there. I wasn't seeing any doctors. You mean physicians for my illness?

Q Naturally.

A I was very nervous and I would get sick, but I never went to a doctor.

Q Did you have a nervous breakdown?

A Practically.

Q Did you see a doctor for that?

A No.

MR. LERNER: Objection. I don't see what relevancy this has. She testified she was ill. What more does Mr. Goidel want?

MR. GOIDEL: When somebody makes false statements, be it under oath or not under oath, I think the Court has a right to view and to take into consideration their propensity to honesty.

THE COURT: Who made the false statement? The letter has -- the letter was written by her husband, not her.

MR. GOIDEL: That is true. As an agent, certainly, for her and himself.

THE COURT: That is a conclusion you draw.

MR. GOIDEL: They are co-owners. They have

the same vested interest. They were husband and wife. They were living together.

THE COURT: May I see the letter, please?

MR. GOIDEL: Yes.

(Pause.)

MR. GOIDEL: Your Honor, if I may be heard for a moment.

On cross examination, especially when the testimony is elicited prior to cross examination, there is just so much any lawyer on cross examination can do. One of those things is that he can do is take any prior inconsistent statement made by or on behalf of the witness, and try to develop from that certain testimony to describe the propensity for honesty and any inconsistent statement that may have been made. Certainly a letter written by the husband which she acknowledges, knows was written and sent and now does not recall if it was sent afterwards or before, but she actually saw it and acknowledges was sent supposedly describing the situation, I think I have a right to go into it.

MR. LERNER: Your Honor, the Court already indicated the letter was prepared and written by her husband. Her husband was on the stand yesterday.

12

He testified that he requested the company buy back his distributorship. At the time, the question should have been put to her husband, and at that time, a question about a prior inconsistent statement should have been asked.

MR. GOIDEL: I can't recall -- I can't say he did not say it -- But I don't recall the statement having been made.

MR. LERNER: That a letter was sent? I don't recall the witness testifying that a letter was sent. I recall the witness stated he requested the company buy back his distributorship.

THE COURT: The only thing I have here is the statement that he never earned any money and requested a refund and didn't get it.

MR. LERNER: That is my recollection.

THE COURT: Just at the very end of the direct examination.

Now, I don't know -- let me see on cross.

MR. GOIDEL: Your Honor --

THE COURT: On cross examination, he stated he still owned a franchise. He attempted to sell it back after he found out he was not going to make any money. This was in November of '72.

13

Silverman-cross/Goidel

MR. LERNER: If the letter says he was happy with the company, and he considers that a prior inconsistent statement, he should have asked the husband and not the wife.

MR. GOIDEL: I am speaking to two witnesses, that is true, with identical interests, who are husband and wife.

THE COURT: No, not necessarily identical interests.

MR. GOIDEL: They were at that time.

THE COURT: Possibly. I will permit you to ask the witness whether she and her husband discussed this getting out of Galaxy. If she can recall when that discussion took place.

Q Madam, do you recall you and your husband discussing getting out of Galaxy Foods?

A Yes.

Q Do you recall when that discussion took place?

A It was shortly after he found out he could not make any money in the company by getting customers. He had no success with that and was disenchanted with the company.

Q Was that before or after December 29, 1972?

14

A (No response.)

Q That is the date of the letter which is marked in evidence.

A Before.

Q Did you and your husband discuss the writing of a letter by him or the preparation of a letter by him before --

A I had nothing to do with the preparation.

Q I am asking you whether you and your husband discussed prior to your husband sending a letter, whether you discussed with your husband that your husband should prepare and send a letter?

A He discussed he wanted to do something to get his money back.

Q Was it his money or your money or both?

A Our money.

Q Did you acquiesce? Did you agree that the letter should be sent?

A Yes.

Q You and your husband jointly came to a decision to withdraw from the business, is that correct?

A Yes.

Q You jointly agreed you would send a letter, is that correct?

A Yes.

Q And this is the letter that was sent, is that correct?

A Yes.

Q Did you and your husband discuss the fact that he was -- he would write in the letter that you were ill and that he needed the funds back in order to provide for your comfort and needs?

A Yes.

Q Did you acquiesce in his doing so?

A Yes.

Q Were you under the immediate care of a physician at that time for any condition whatsoever?

A We couldn't afford to go to a doctor.

Q I am not asking that, I move to strike that.

I am not asking what you could afford, I am asking whether you were?

A No, I was not.

Q You did attend nursing school at that time?

A Yes.

Q There are doctors at the nursing school and at the hospital with which the school is associated?

A Yes, there are doctors.

Q Did you ask to be put under the care of any

physician at the hospital while attending nursing school?

A No, I did not.

Q Your husband, you say, was disenchanted with Galaxy because he could not enlist people to apply for franchises?

MR. LERNER: Objection.

A No, I said he could not earn any money from getting customers in the company.

Q Why --

A Customers that would buy food and he would earn a commission on.

(continued next page.)

Q Did he try to get customers?

MR. LERNER: Objection. That is not what the testimony is. He couldn't turn commissions by getting customers, not that he could --

MR. GOIDEL: Well, let me go on with the witness.

Q Which is it, he could not obtain customers or that he could not get commissions on customers which he did obtain?

A He was told by a Mr. Mark Glasser, I was not present at the time of the conversation --

Q Your husband was acting in behalf of you and himself?

A Yes.

Q Mr. Glasser was an officer of the corporation?

A Yes.

Q You say your husband was told something, do you know what he was told?

A He would not be able to -- my husband wanted to know what area he would service. And he was told within a certain radius of the warehouse, and they had combed that area already. The company, themselves, had combed that area already, and they were asking the franchise owners to go in again to see what customers they

might get.

Q Did your husband try to get customers?

A No, it was explained to him that the company had already gone in there and gotten what they could.

Q Did your husband try to get customers anywhere else?

A Yes.

Q Where?

A In our neighborhood.

Q Did you try to get customers?

A No.

Q Was your husband told that if he did get customers, that he would not be paid commissions?

MR. LERNER: Objection, that calls for hearsay.

Q Are you aware of any communication to you and your husband, verbally and written, as joint owners of that franchise, that you would not earn commissions notwithstanding your acquiring customers for food?

A You have to repeat it.

Q Were you and your husband, as owners of a franchise, advised in any way that even if you got customers for food, you would not earn commissions on the sale of that food?

A I don't remember. I really didn't get involved in the company that much. It was really my husband that did.

Q Madam, the first contact with the company was through you?

A Yes, but after that I let him handle everything that had to do with the company. He made the contact with the people after that.

Q May I ask you this question, did you and your husband, while making loans or attempting to make loans, have a discussion about any bank accounts which you had?

A When we made out the loan applications.

Q What did you say or what did he say?

A If the loan application asked where you had a bank account, I told him -- or I filled it out myself and put down where we had the account.

Q Did your husband know where you maintained the account?

A Maybe not. I kept all the records.

Q Did you discuss this case with your husband yesterday while walking out of this courtroom?

A (No response.)

Q Did you discuss his testimony?

A Not really.

Q At all?

A Yes, we did.

Q Tell me exactly what he said to you and what you said to him?

A He told me about the bank account. I know he was not familiar with how much money I had or where the accounts were. He knew, I guess, the name of the bank, but he wasn't familiar with it.

Q Is that what you discussed with him yesterday?

A We really didn't discuss much at all.

Q I'm asking you.

A I'm telling you.

Q You did discuss that aspect of his testimony?

A Yes.

THE COURT: Was the savings bank account in your joint name?

THE WITNESS: No, my name.

THE COURT: Were the deposits in that account--how did the deposits in that account come about?

THE WITNESS: I deposited all the money.

THE COURT: Where did the money come from?

THE WITNESS: I had a part-time job while going to school.

THE COURT: Did it represent the proceeds of

that part -time job of yours?

THE WITNESS: Yes.

THE COURT: Did it represent anything you got from your husband?

THE WITNESS: No.

Q How about the checking account?

A That was from my husband's earnings.

Q Where was your part-time job?

A In an office in an apartment building for a paint contractor.

Q What did you earn part-time?

A $25 a week.

Q Did you also discuss with your husband after leaving this courtroom yesterday, your Social Security number and the testimony given with regard to that?

A All he did was ask me what my number was.

Q Did he tell you why he wanted to know what your number was?

A He said he was asked.

Q Did he tell you in what reference he was asked?

A It appeared on something, he wasn't sure what the number was.

Q Did he tell you what it appeared on?

A The W-2 form.

Q Did he tell you which W-2 form?

A The W-2 form that is in evidence here.

Q Did he tell you that he could not explain how your Social Security number appeared on that W-2 form?

A He asked me if I had given it to Mr. Shevack, and I said I don't remember giving it to him.

MR. GOIDEL: Your Honor, I don't think I have any further questions of this witness at this time.

THE COURT: Fine. Is there any redirect?

MR. GARMANSKY: Can we have a few seconds?

THE COURT: Yes.

(Pause.)

(continued next page.)

MR. LERNER: No further questions.

THE COURT: All right.

We will take a 10 minute break.

(Recess taken.)

MR. LERNER: Your Honor, the Commission rests its case in chief.

MR. GOIDEL: Your Honor, I would normally take time at this time to make the usual motions and to elaborate upon those motions, but I understand that it will be deemed that I have made them and that I will not give any long dissertations at this point, preserving our right at the end.

THE COURT: Just state the motions you wish to make.

MR.GOIDEL: Yes, your Honor.

THE COURT: For the record.

MR. GOIDEL: Right.

THE COURT: It will not be necessary to engage in any argument at this time.

MR. GOIDEL: Fine.

I move at this time, your Honor, to dismiss the complaint against both Messrs. Kirsch and Shevack, on the grounds that a prima facie case has not been established. There has been no

demonstration of any fraud committed by them, and that each of the witnesses who have testified here today have ndicated that they were fully aware and cognizant of all the facts relative to the operation of Galaxy Foods, Inc.

I also feel that there has been sufficient discrepancy between the various testimonies of the witnesses produced, as to warrant that their statements be given little credence and that a preponderance of the evidence cannot, therefore, be deemed, even in the absence of any testimony by the defendants, to have established a prima facie cause of action.

THE COURT: Well, I will reserve decision on those motions.

MR. GOIDEL: Thank you, sir.

Your Honor, I call Mr. Shevack, Arthur Shevack, to the stand.

A R T H U R C R A I G S H E V A C K, having been first duly sworn by the Clerk of the Court, was examined and testified as follows:

DIRECT EXAMINATION

BY MR. GOIDEL:

Q Mr. Shevack, you are aware of the fact that

if any answer given by you would appear to involve you in the commission of a crime, that you would have the right to plead your rights under the 5th Amendment of the Constitution of the United States; is that correct?

A Yes.

Q You and I have discussed the facts of this case at length; have we not?

A Yes, that's correct.

Q We have reviewed the testimony of various witnesses who have been produced by the Securities and Exchange Commission; have we not?

A Yes, we have.

Q I even spoke with you this morning concerning the testimony taken yesterday, of several witnesses, is that correct?

A Yes.

Q Notwithstanding that, you have taken the stand, is that correct, sir?

A That's right.

Q Mr. Shevack, what was your first association with Galaxy Foods, Incorporated? What time?

A I estimate, approximately in June I met Artie Lee, not for the first time, but I met him at a location in Brooklyn, which he was holding, I later found

out to be an opportunity meeting.

THE COURT: When you say, "June", June of what year?

THE WITNESS: I believe it was '72.

Q Had you --

THE WITNESS: Approximately.

Q Had you, prior to that meeting with Mr. Lee around June of 1972, ever heard of Galaxy Foods?

A Yes, I had.

Q Prior to that time?

A Yes.

Q Who first mentioned Galaxy Foods to you, prior to the June meeting in 1972?

A Mr. Lee, Artie Lee.

Q What did he say to you, what did you say to him on that first occasion that you met?

MR. LERNER: Could we have a time?

MR. GOIDEL: He said in June or just prior to June.

Q Is that correct or --

A This is on the first occasion when I met Mr. Lee in reference to Galaxy Foods?

Q Yes, sir.

A At that time I was there-- I think it was the

Camilla Room on Avenue U and I walked in and he was inside, and I had previously known him, so I was discussing it with him.

He invited me inside to stick around a while to see what he was doing.

Q When was that, sir, so that we are clear on the approximate time?

A Approximately beginning of June, I believe.

Q Of 1972?

A Of 1972.

Q What did he say to you, what did you say to him, with regard to Galaxy Foods?

A Well, he invited me inside the room. He said he's got a great company going, a lot of money to be made. You know, come inside, see what I'm doing, I know you'll like it. You know, it fits you like a glove. You know, that type of thing.

Q And did you --

A So I was curious. Yes. I was curious as to exactly what the heck he was doing.

I had gotten a phone call from him maybe a year earlier, which I never responded to, and, you know, curiousity, I walked inside. I sat down and I viewed the presentation.

I don't know if I came in at the very beginning. I really don't recall, but I saw maybe two hours worth of what they were saying. I assume it was pretty close to the beginning.

MR. LERNER: Your Honor, I object to the answer because it is not responsive.

The question was, when did you first hear of Galaxy Foods. He's now testified he got a letter from Mr. --

THE WITNESS: No, no letter.

MR. GOIDEL: A call the year before but he did not return the call.

THE COURT: To which he did not respond.

MR. LERNER: Forgive me.

Q Mr. Shevack, try to respond to the questions that I ask.

A All right.

Q Without giving me too much elaboration.

You say you spent about two hours at that meeting?

A Yes.

Q Did you speak with Mr. Lee after the meeting?

A Yes.

Q Would you tell us what you and he discussed after the meeting?

A Well, he asked me to join the corporation, to purchase a distributorship, and I told him, you know, $5,000 was a lot of money and did he really have intentions of, you know, carrying out the promises he was making.

Q What did he respond to those questions?

A He says, you know, as -- as everybody said during the meeting, he responded, you know, affirmatively.

He kept telling that yes, we can do everything we say we can do, it's going to be great, the percentages that you can earn, you can get customers, we're really going to make deliveries. Everything is set up. It's all ready to go.

You know, that type of thing.

Q Did you discuss with him how you would finance the purchase of a distributorship?

A Well, he invited me for coffee and we spent approximately an additional 2 to 3 hours and he was explaining me how the corporation would be able to carry through on the retail operations. You know --

Q But did he specifically discuss with you how you would finance your purchase of a distributorship at that meeting?

A Yes, he did.

Q And what did he say to you with regard to how you would purchase your distributorship?

A He says, "I'd be able to work it off."

In other words, I could sponsor someone into the business who would purchase a franchise. He would give the commission to me. I'd have to use his name in this -- sponsoring the individual in, but when I accumulated 5,000 dollars, I would give it back to him and then purchase a franchise.

Q Did you ever use that method with any person with -- whom you sponsored into the business?

A Yes, I did.

Q Where you allowed them to purchase in through you by their obtaining prospective distributors and field managers?

A Well, sure.

Q Now, sir, did you execute an agreement with Galaxy Foods under which you purchased a distributorship?

A Yes, I did.

(continued next page.)

Q When did you actually purchase that distributorship?

A If I recall correctly, approximately mid-July. I actually purchased for $5,000 the distributorship.

Q Did you have any other relationship or association with Galaxy Foods, other than as a distributor?

A No, none whatever.

Q Were you a shareholder of the corporation?

A Never.

Q Were you a director of the corporation?

A Absolutely not.

Q Were you an officer of the corporation?

A No.

Q Sir, you attended that first opportunity meeting to which you were invited by Mr. Lee? Did you ever go to any other opportunity meetings before subscribing to a distributorship?

A Yes, I did.

Q How many different meetings did you attend before you actually signed up to become a distributor?

A Approximately 10, 15. In that vicinity.

Q Were these particular meetings conducted by particular individuals associated with Galaxy?

A Yes.

Q Can you name the individuals who ran or conducted the meetings known as opportunity meetings, that you attended?

A Mark Glasser, Luigi Gordagno, Artie Lee, Charlie Hurwitz, Steve Roth, Bruce Katz.

There were others. Ralph Martin.

I can't recall any more names at this time.

Q Now, prior to your actually signing up as a distributor yourself, that is, executing one of those contracts, did you enlist individuals as prospective purchasers of their own franchises or field manager positions?

A Yes,that was the agreement with Mr. Lee.

Q When you would bring an individual to a meeting --

MR. LERNER: Objection. There has been no --

MR. GOIDEL: Withdrawn.

Q The people whom you solicited, did you go to meetings with them?

A Yes.

Q Did you sit with them?

A Occasionally, yes.

Q Would you describe for us how these meetings were conducted?

A How they were conducted? Well, they would

normally be at some type of banquet room, ballroom or reception room in a particular hotel that I assume they arranged for previously. They would publish a list of where it was so you knew where it was to be. Hopefully it didn't change when you got there.

You would bring whoever it was with you or have them meet you there or whatever the case may be. There were people at the door who you'd have to -- you know, you'd put their name or they'd put their name and they'd ask who the sponsor was and then they'd try and connect it to somehow, unless you remembered the individual or were with him at the time.

You'd sit down in a meetingroom and normally, someone would get up there and start it off by saying, you know, "Good evening, ladies and gentlemen, welcome to the world of Galaxy Foods" and the emeeting would start.

The various speakers would go up and do their part.

Q At these meetings, sir, were there discussions as to how one could earn monies?

A Yes.

Q How many ways of earning money were discussed?

A Basically two.

Q Can you describe them for us, what was said?

A Well, there were two franchise positions, two distributorships. One a distributor and the other one a field manager.

Both basically operated the same other than the fact of the commission structure. The primary reason that they were selling you a franchise was that you would be able to go out and acquire customers who the company would then deliver the merchandise to. You would receive your respective percentages on whatever they spent and, therefore, you'd be able to earn money by soliciting business for people who wanted to get food delivered.

The other method was that during the time that they had franchises available, they offered the distributorships and the field managers an opportunity to earn a commission on the people they found who also wanted to purchase a franchise or a distributorship.

Q Sir, how long did you remain in Galaxy Foods, remain associated with it?

A It's hard to give specifics; but approximately 6 months. Maybe less.

Q If you entered in June, sir, what is the best recollection you have as to when you terminated your association with it?

THE COURT: I wanted to clear something up.

MR. GOIDEL: Yes, sir.

THE COURT: As I understood it, he met Mr. Lee in early June, first part of June?

MR. GOIDEL: Yes, sir.

THE COURT: It was in mid-July that he actually signed up with his own distributorship?

MR. GOIDEL: That is correct, sir.

THE COURT: I take it, when he said he attended some 10 or 15 meetings, he is speaking about the month and a half between the first of June and the middle of July?

THE WITNESS: Yes, that's correct.

THE COURT: Is that right?

THE WITNESS: Yes.

THE COURT: So that when you say "when did he become part of Galaxy", it is a little unclear as to whether he considered himself part from the time he started in early June or when he actually signed his distributorship agreement in mid-July. That is what I would like to have cleared up.

MR. GOIDEL: Fine.

BY MR. GOIDEL:

Q Sir, did you consider yourself a part of Galaxy when you started in June to enlist people to join or

did you consider yourself part of Galaxy in July, when you actually subscribed an agreement?

A In July. I wasn't registered previously with the firm in any capacity at all.

Q You were going to receive some benefit between June and July?

A Yes.

Q Isn't that correct?

A Directly from Mr. Lee.

Q That was in the nature of earning a franchise?

A Yes.

Q So that you would not have to reach into your pocket and pay $5,000?

MR. LERNER: Objection, your Honor. I assume the same objection as to leading questions.

MR. GOIDEL: I --

MR. LERNER: Please, Mr. Goidel. I want to get this one comment in.

THE COURT: Try to observe that.

MR. GOIDEL: Fine. I think it's established.

BY MR. GOIDEL:

Q Now, sir, when is the last time that you recall in any way being associated with Galaxy Foods?

A In December of '72.

Q Can you describe for us how you terminated your association?

A I sold my franchise.

Q Would you describe for us the method under which you sold your franchise?

A Well, I had worked very hard and tried to establish a business for myself, and I had customers at that time. I had what they called field managers in my franchise organization.

So I went to various people in Galaxy Foods and asked them -- it was going at that time, for $7,000. I asked them if they'd like to purchase mine at a discount. I was willing to, you know, sell it for less than it was going for, so I could receive some money for it.

I did get a lead from someone there, and I did end up selling it to a relative of somebody who already was in Galaxy Foods.

Q Would that be a relative of Mr. Padilla?

A Yes.

Q How much did you sell your franchise for, sir?

A Well, the actual sales price was $6,000, but $500 of that had to go to Galaxy Foods, as a -- a thank you, I don't know what you would call it, as a transfer fee.

Q Could you describe for us the circumstances under which you resigned?

A Well, prior -- they were telling us they're going to get customers, they're going to get customers, they're going to get the operation going, and it had been postponed continuously month after month. They just kept coming -- another delay, another delay.

Q By "customer," you mean customers for what?

A For food, customers to purchase food.

And I endeavored to get these customers for the food and we were under the assumption, as everybody was, that we're supposed to receive a commission on it. That's why we purchased one of these distributorships.

And in actual fact, they did deliver, and we never received any commissions on these customers who bought food.

Q Did you solicit customers for the purchase of food?

A Yes, I did.

Q Did you take orders for the purchase of food?

A Yes, I did.

Q Do you know approximately how many orders were submitted to Galaxy from customers of yours?

A Approximately, I'd say, 200 orders were submitte

How many actually got delivered, I don't know.

Q These orders that you took, can you describe for us how you took these orders?

A Door to door.

Q You, personally?

A Yes.

Q Anybody assist you?

A Yes.

Q Who assisted you?

A A Mr. Cancilla assisted me; my wife assisted me; some of my relatives assisted me. You know, whoever I knew that was willing to assist, assisted.

Q Would you tell us who Mr. Cancilla was, at that time, what relationship he had to you?

A Well, Mr. Cancilla had been a personal friend, and when I joined Galaxy Foods, I asked him if he wouldn't mind helping me. He endeavored to do so and the busier we got, the more help he actually gave me.

Eventually he became my partner.

Q Was that partnership arrangement ever evidenced in writing?

A Yes, it was.

He gave me half of what I paid and I submitted partnership papers to the corporation, to register it as a

partnership.

Q When did you submit the papers to the corporation to register your distributorship as a partnership?

A I would estimate, 30 or 45 days after -- no. Wait a minute. Let me correct that.

Let me -- I would say approximately two weeks after I became registered as a distributor.

Q When did you first --

THE COURT: You mean, about the first of August of '72?

THE WITNESS: June -- Yes, approximately the first of August. Yes.

Q When did you first start soliciting customers for the purchase of food?

A Well, we started talking to people about the possibilities that they may be able to use the service around September and ended up actually starting to take orders November and the latter part or the beginning part of December.

Q When did you first learn that you were not going to receive commission on the sale of food?

A This was about the latter part of December.

Q Sir, you testified that there were two ways to earn money discussed at the opportunity meetings; one was the

sale of food. The other was the sale of franchises or field manager positions; is that correct?

A Yes.

Q Did you sell any franchises or distributorships to anyone?

A Yes, I did.,

Q Would you describe for us how many you actually sold or took applications for?

A I believe I turned in approximately 10 applications to the corporation, you know, for approval on a sale.

Q Did you realize any money from the sale of those franchises?

A Yes.

Q How much money did you realize totally on the sale of all of those franchises?

A A little over $11,000.

MR. LERNER: Excuse me. Does that include the sale of his own franchise?

MR. GOIDEL: We'll go into it.

MR. LERNER: Okay.

MR. GOIDEL: The sale of his own franchise is not a commission.

Q Are those all of the commissions that you

earned, during the period of time that you were associated with Galaxy Foods?

A Yes.

Q Did you retain all of those commissions for yourself?

A No, I did not.

Q Did you share those commissions with anyone?

A Yes, I did.

Q With whom did you share the commissions?

A 50 percent of everything paid to me went to Mr. Cancilla as my partner.

Q Did you evince this on any income tax returns filed by you and Mr. Cancilla?

A Yes, sir, I did.

Q Youindicated on those returns, sir, that you retained half of the proceeds of the $11,000 plus; is that correct?

A Yes.

Q Sir, was there applauding, clapping, cheering or any other means or form of enthusiasm demonstrated at opportunity meetings?

A Yes.

Q Could you describe for us, particularly when you had occasion to witness any form of enthusiasm?

A Enthusiasm was displayed at each and every meeting that they held, for whatever purpose.

Q Would you describe for us what you mean by "enthusiasm"? Or the displaying of enthusiasm?

A Well, there were people who were smiling, that had a happy face on. They applauded. Occasionally someone may have cheered. I don't know if you'd call it a cheer. You know, they seemed excited.

Q Was it a circus? What we would describe as a circus?

MR. GARMANSKY: Objection, your Honor.

What does he mean by a "circus"?

MR. GOIDEL: Well, I think we all know a -- what a circus is.

MR. GARMANSKY: No, I don't know what a circus is, Mr. Goidel.

MR. GOIDEL: Do you want me to clarify it?

MR. GARMANSKY: Yes.

Q Was there running up and down aisles?

A Yes, there was.

Q People generally got up and ran up and down the aisles?

A I'd say so, yes.

Q Okay.

Q Sir, did you speak at any of these meetings?

A Never.

Q Not one?

A These are opportunity meetings you're referring to?

Q Yes.

A No, sir, never.

Q There were also step-up meetings, is that correct?

A Yes.

Q Could you tell us what a step-up meeting was?

A That was a term used for a Sunday, when they would take you on a tour of the facilities and they'd bring you down to the offices where the supposedly executives or the board of something would get together, and they'd explain a little more about the business, how you could earn more money, that type of thing.

Q Did they also get money out at those meetings, checks?

A Yes.

Q Did you receive your checks at step-up meetings?

A Yes. That was the procedure.

Q What is the largest check you ever received at a step-up meeting?

A $2,000.

Q Did you ever receive a check for $6,000?

A I wish I did.

Q Did you or did you not?

A Never.

Q Did you ever show anyone a check for $6,000 received by you by -- from Galaxy Foods?

A I never had one to show. The largest check I ever got was $2,000.

Q Did you ever show a check to anyone from anyone, from any other firm?

A No.

Q For $6,000?

A No.

Q So that there is no question about what we are discussing, when I speak of you in relation to the receipt of funds, I mean you or anyone else receiving funds in your behalf, be it Mr. Cancilla or anyone else who may have received a check in your behalf or in the behalf of both you and Mr. Cancilla. Did either of you ever see a $6,000 check or receive one?

A No. The largest check we ever got was $2,000.

Q Sir, during the course of this trial, one witness in particular, a Mr. McLean, testified to having seen

a check for the amount of $6,000, shown by him to -- shown to him, rather, by you, at a step-up meeting.

MR. GARMANSKY: Your Honor, I object. That is incorrect. Mr. McLean never testified he saw a $6,000. He said it was a $3,000 check.

MR. GOIDEL: Oh, no.

THE COURT: Let's find his testimony.

MR. GOIDEL: Oh, no.

THE COURT: It is always best before confronting a witness with a statement to go to the record, we -- so we won't have to waste time trying to straighten something out that everybody finds to be inaccurate.

MR. GOIDEL: Your Honor, I'll straighten it out in my brief, and I will withdraw the question.

(continued next page.)

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Q Sir, may I ask you this question; in light of what Mr. Garmansky has said, did you ever receive a check for $3,000?

A I repeat, I never received a check larger than $2,000 under any circumstances, from Galaxy Food.

Q That $2,000 was part of the aggregate of a little over $11,000 which you say you received in all?

A Yes.

Q In addition to the $11,000, which you received as commissions, did you also get the additional funds from the sale of your own franchise when you terminated your association or was that sum also part of the $11,000?

A I received that sum back but I also had to purchase a franchise so it wiped itself out.

Q Included in this $11,000 plus, you received were monies that you earned when soliciting applicants, while using Mr. Lee's name?

A (No response.)

Q Do you understand?

A No, I don't think that it is correct. I earned $11,000.

Q In cash in hand?

A In commissions. A little over $11,000 in commissions that I received. Prior to being registered with

the firm, in July, I don't believe they added that to my return -- I don't know if that was in my return or not. I couldn't testify to that.

Q But you did receive an additional 5500 dollars then, at the end?

A Yes, when I sold it.

MR. LERNER: That check did not come from Galaxy?

Q Who did that check come from?

A From the individual who purchased my franchise. It didn't come from Galaxy Foods.

(Pause.)

Q Before you actually signed a contract which made you a registered franchisee, did you get monies in hand from anyone as consideration for the work that you were performing in soliciting applicants?

A Yes.

Q Was that given to you?

A Yes.

Q What did you do with that money?

A It was my choice whether to purchase the franchise or remain in my present status as not associated but really earning the same money as buying a franchise.

Q You took that money and used it to purchase

your franchise?

A Yes, the food sales was what I was joining for.

MR. LERNER: Your Honor, I think I have an objection to the answer that $11,000 was the total sum received as commission because when he sold the franchise, he would recoup the commissions he --

THE WITNESS: I must object personally because that commission was not paid to me by Galaxy Foods. That commission was paid by Arthur Lieberman directly. It was his name being used, he was the sponsor. The commissions were paid to him and he gave me the money.

Q You gave it back to him to purchase your franchise?

A Yes.

Q Now, sir, would it be fair to state that in toto, you and Mr. Cancilla realized in cash, 11,000 plus dollars, approximately 11,500 dollars in commissions from Galaxy, and an additional 5500 dollars on the sale of your own franchise to Mr. Padilla's relative?

A Yes.

Q Did you get any other type of money for any purchase from Galaxy?

A No. That is more, in fact, than I earned.

Q Did you have cards printed -- strike that.

Did you have any other expenses associated with --

A Yes.

Q Let me finish the question first.

Did you have any other expenses associated with the earnings of commissions and the sale of food?

A Yes.

Q What were those expenses?

A Numerous. One of which to bring a guest with you on Sunday. To just have the possibility that he may be able to purchase a franchise and would purchase a franchise, you had to pay $5 to get him in there.

Q I didn't know about that, sir, tell us.

A You had to pay $5 for every individual you brought on Sunday. If he had a wife it was $10. If you came it was $15. If your brought your wife it was $20.

Q Who did you pay the money to?

A This was given, I guess, for room rental or I don't know what, but that was the requirement.

Q In other words, Galaxy didn't lay out the money or absorb the expense, you had to pay them?

A Yes. As an independent salesman for the use

of their facilities. In addition -- shall I go on?

Q Sure.

A You had to pay dues to use the banquet rooms they were renting.

Q Well, to whom did you pay the dues?

A One of the Galaxy -- I wouldn't say officials -- yes, I guess it was an official, Ralph Martin, or one of those people, were sitting at the door. That would cost $30 a month. Not to mention the gas for running around. If you bring a guest and he wants a drink or something to eat, God forbid the guy should be hungry, there goes a meal for $20. You can't be chintzy about it. We had to buy the literature. You had to purchase the catalog or what they called a closing book.

If you liked a book with some pictures in it, explaining what the company was all about. I believe it's right there (indicating.)

The brown one on the desk. That book would cost $5.

Q You are referring to a book marked plaintiff's exhibit 11?

A Yes.

Q How many of these did you purchase?

A I bought one for myself, I bought one for my

partner and naturally, when an individual was interested in it, what you are showing him, if he liked one, you wouldn't tell him to buy it himself, you purchased it for him. I brought many people down who didn't buy, but had a book.

Q Can you tell us approximately how much you spent on books of this type?

A Approximately $100, at least.

Q I also show you plaintiff's exhibit 3.

A We had to buy those also.

Q How much did you have to pay for these?

A Honestly, I don't recall the price. They were selling for approximately $1.50 or $2.50, around that area.

Q How many of those did you purchase?

A 30, 40.

Q Did you hand them out?

A Yes, most of the time I did.

Q Did you have any other expenses?

A Well, the contract, I think they are a quarter apiece, and I think I went through hundreds of those things. I couldn't even estimate how many of those I used.

Q Now, was anything given to you for nothing?

A (No response.)

Q As a sales gimmick or sales brochure?

A For nothing?

Q Yes.

A No. I even had to buy a badge.

Q A badge?

A To let me get into the facility, they charged me $5 to get in.

Q You are talking about a name tag to wear on your jacket?

A Right.

Q Did you ever speak at a step-up meeting?

A No, I never did.

Q Did you ever hear of training sessions?

A Yes.

Q Did you ever speak at a training session?

A No.

Now, there were two types of training sessions that I recall. There was one that they gave the distributors who joined, and then there was one, I guess, for the association which was in the evening.

Q One at a time. Did you ever speak at the first type, the training meeting for distributors?

A No, only officials spoke there.

Q By officials, you mean officials of Galaxy?

A Yes.

8

Q Officers, directors?

A I wouldn't even say officers, directors. People with some stature in the company.

Q How about the other type of training sessions, when you called the distributors -- what? Association?

A Association meeting.

Q Did you ever speak at that?

A On one occasion, yes.

Q What was the topic of your conversation?

A Mr. Mark Glasser had invited me down and had asked me to speak 5 or 10 minutes -- I believe it was on a Friday evening, and he asked me to come. It was about 9 o'clock at night. 9:30 at night. And he had asked a couple of people to attend. You know, just elaborate on how they operated their particular distributorship. I did.

I went there that evening. You know, I explained how I operated my business.

Q Did you ever hear the expression, "cold canvas" or "cold canvassing?"

A Yes.

Q Would you tell us what cold canvassing is?

A Cold canvassing is like the Fuller Brush Company, you approach someone you don't know, who you never seen before, and talk to them about purchasing your product.

You know, door to door, or whatever it may be.

Q Did you use that expression during the course of your 5 or 10 minute speech at the distributors' association meeting?

A No, I did not.

Q What did you discuss at that meeting that you spoke of?

A The particular terminology -- it's hard to use words, cold canvassing isn't the type of word I use. I would say approaching an individual, or something like that. Talk to someone about joining the company. That is the type of vocabulary that was used.

Q Without having used the term, was the subject matter that you discussed what we would designate, perhaps, as cold canvassing?

A No, I don't believe it would be. I didn't discuss that particular topic.

Q Tell me what it is you discussed at that meeting, if you can recall?

A To the best of my knowledge I was discussing, after the opportunity meeting, the way to explain if a man was interested in the business opportunity. The way to explain what was just written on the blackboard during the presentation. It was done so fast many people were

10

confused.

MR. LERNER: Is this an opportunity meeting, now?

Q Are you talking about what you discussed at the training session that we are talking about?

A Yes. Not even a training session, the association's training session in the evening.

Q Is that what you discussed there that evening?

A Yes.

Q How many times did you speak at the association training session?

A Once. Not more than 15 minutes.

Q Is that the only time that you gave a presentation of any type at any meeting of or any meeting associated with Galaxy Food?

A Yes, never before or after.

(continued next page.)

DIRECT EXAMINATION

BY MR. GOIDEL (Cont'd):

Q Now, sir, aside from prsentations of that type, you did however have discussions with people on an individual basis or a group basis; is that correct?

A Yes.

Q When would such discussions take place?

A After the Opportunity Meeting or after the Step-Up Meeting.

Q When you had a prospective purchaser of a franchise, did you always escort that person to an Opportunity Meeting?

A Always? I would have to say no.

Q Well, were you in attendance whether they met you there or whether you escorted them, were you in attendance at every meeting where any one of your guests would be present?

A Yes.

Q Youwould listen to the presentation being made at the Opportunity Meeting?

A Yes.

Q Did this presentation vary from meeting to meeting?

A Very slightly.

Q Did they use a blackboard?

A Yes.

Q They wrote figures on the blockboard.

A Yes.

Q Did they follow a script?

A 99 per cent of the way through, yes.

Q Did you have anything to do with the preparation of the script?

A No.

Q Was that script, if you know, in use prior to your affiliation or association with Galaxy, if you know?

A Yes.

Q Now, sir, you said that following Opportunity Meetings, people were at times confused?

A Yes.

Q Would you tell us -- can you tell us any specific instances that you can recall where individuals spoke to you and evidenced their confusion?

A Well, many of the guests that were there were confused. I recall people who I brought down were confused. I remember Mr. McLean was confused.

Q Who is Mr. McLean?

A Mr. McLean is a field manager in Galaxy Foods.

Q Who sold him his field manager distributorship

or franchise?

A Galaxy Foods.

Q Who took the application?

A I did.

Q He was one of your guests?

A Yes.

Q Would you tell us what Mr. McLean evidenced confusion over? Can you recall when approximately that conversation took place?

A It is difficult. I can only give you estimates, between August and October. You know, I can't narrow it down any more than that.

Q Where did Mr. McLean speak with you in regard to his confusion?

A I believe it was on Flatbush Avenue, in Brooklyn. Not the office. They had rented a room there.

Q Who is they?

A Galaxy Food.

Q Yes?

A And it was after one of the Opporutnity Meetings that -- it was his first time down. He came over and -- they had used him different types of instruction and he was confused how he would earn some of the sums they were discussing.

Q Do you recall what it was that you said to him?

A He said, "It's a lot of money. How can I earn this much money?"

I explained, "You would have to do X, Y and Z, if you got this many salesmen, if they got this many customers, if they got this much money, you have the possibility of earning this much." I gave him proportion, one customers to 1,000 customers. I forget the numbers at this point.

Q Did you ever explain that it was possible not to earn a penny?

A Sure. We told him, "If you don't work, you can't earn. Your earning is depending on how many customers you get. If you sell a franchise, it's up to him."

Q Sir, did you ever take Mr. McLean to a bank?

A No.

Q Did you everassist Mr. McLean in filling out any bank forms for a loan?

A No, I did not.

Q Did you ever suggest to Mr. McLean that he go to a bank for a loan?

A I think at one point he asked me how would I get the money to join. I explained he could borrow it from friends, neighbors, relatives, finance companies, bank. I told him to look in the newspaper, there are ads every day. He asked me to lend it to him. I told him I wouldn't do it.

We already arrived at an agreement where I would let him join by the same manner I was entitled to join. He was tight for money. He didn't have a high-paying position and rather than put an added burden on himself, I will allow you to earn a commission on someone you bring down who decides to join. When you accumulate the price, then you will be recognized like I was.

Q Did you ever get paid a commission by Galaxy Good on Mr. McLean's membership fee in the organization?

A I did but I was forced to turn it back over to the corporation.

Q Would you describe that for us, please?

A He finally accumulated $2,000 from finding three individuals who were to join the corporation, and I remember, I think he gave me a deposit of some amount, one or two hundred dollars. I should have gotten a commission of $750 or $800 on Mr. McLean, but Galaxy said they needed it to recognize him as a franchisee. To this date that matter is not cleared up in my mind. I never received a commission on Mr. McLean.

When he joined I received a check but that was given back to Galaxy.

Q The very same check?

A Yes.

Q Sir, were there ever any discussions anywhere that you heard or overheard, related to the question of borrowing monies in order to sponsor the purchase of a franchise?

A Could you repeat that?

(Question read.)

A Yes.

Q Where did you hear or overhear such a conversation?

A After the Opportunity Meeting normally, or every -- at the Step-Up Meetings there was always groups of individuals standing around talking about how to get this kind of money or that kind of money or where he's getting his money from, who is lending it or whatever is going on. You know, another guy somewhere would be bringing somebody in -- in order to earn something like Mr. McLean, as I did. They were talking about how much they accumulated and if it were $500 and you know, it was always going on there.

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(Continued on next page.)

Q Did you ever tell Mr. Simmons -- by the way -- withdraw that.

Do you know a Mr. Simmons?

A Branch Simmons, I know.

Q Did you ever tell Branch Simmons to borrow money?

A No.

Q Did you ever take him to a bank?

A No, I did not.

Q Did you ever write out an application for a loan for him?

A No.

Q Do you know whether he did borrow money?

A I don't know whether he borrowed it or he had it or what. I know he paid me for a franchise.

Q Mr. Simmons, sir, previously testified that you wrote out an application form for him which he signed.

I'm asking you, sir, didyou write out any application form for anything whatsoever, be it a bank loan, a finance company loan or anything?

A The only application I filled out for Mr. Simmons was his contract upon joining Galaxy Foods, to turn into the company.

Q Sir, two other people, making it four in all,

2

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have also said that you assisted them in making loans or in inducing them to obtain loans.

Are you familiar with a Mr and Mrs. Silverman

A Yes.

Q Well, you say that in sort of a peculiar way, sir. When did you first meet them?

A They were introduced to me through a mutual acquaintance.

Q By whom, sir?

A A mutual acquaintance.

Q Who was the mutual acquaintance?

A It was a Terry Vorano.

Q Who is Miss Vorano?

A She has now become my partner's wife.

Q By "partner" you mean Mr. Cancilla?

A Yes.

Q What is Miss Vorano, by vocation?

A She's a registered nurse.

Q Now, sir, Mrs. Silverman has testified earlier today that you called her in order to arrange with her to come to an opportunity meeting.

MR. LERNER: Objection, your Honor, the testimony does not state that.

MR. GOIDEL: Yes.

MR. LERNER: Her testimony was that he called her husband.

MR. GOIDEL: That's not the testimony. If I had it here, I'd be happy to read it.

All right, sir. I'll rephrase it in the alternative, then, with your permission.

BY MR. GOIDEL:

Q A statement to the effect that either you called her husband, that Mrs. Silverman's husband, or her, to arrange for them to accompany you to an opportunity meeting; is that statement correct, sir?

A No, it is not.

Q Would you tell us whether -- tell us how you first learned of Mr. and/or Mrs. Silverman?

A The first time I even knew they were alive was when Terry Vorano, who was a registered nurse, also working with Mrs. Silverman, Terry Vorano called me and explained to me that there was someone who heard that I was in the Galaxy Foods and they believed it to be a good business, they wanted to know more about it, come down to an opportunity meeting; and I explained to them, you know, my schedule was busy for a while, but if you'd like to set up an appointment for them to come down and see me, I can give you the location, or if you want, I can pick them up,

if you'd -- I gave them a date, somewhere, if they're free on this night, I'll be happy to stop by and give them a lift down.

Q Who was this conversation that you had with?

A This was with Terry Vorano.

Until I went to their house, I had never seen, heard nor spoke to them. I didn't even know where they lived until Terry Vorano gave me the address.

Q Mrs. Silverman also testified to the effect that you, she, her husband, Mr. Cancilla and your wife went to that opportunity meeting to which they first were escorted. Is that correct?

A No.

Q In what respect is that not correct?

A Myself and Mr. Cancilla were there.

Q Was your wife present?

A No, she was not.

Q Had you ever spoken to either Mr. or Mrs. Silverman before you went to pick them up?

A No. I didn't even know them.

Q Now, sir, I show you a document marked as plaintiff's exhibit 37. Have you ever seen that or a copy of that before?

A Yes.

BEST COPY AVAILABLE

5

Q When for the first time did you ever see that or a copy of that before?

A This morning in your office.

Q Sir, I want you to look carefully at that. Is that your handwriting?

A No, this is not my handwriting.

Q Did you and I go over that today, this morning?

A Yes.

Q Are you saying under oath that that is not your writing, any part of it?

A No, this is not my handwriting.

Q Sir, I show you this, plaintiff's exhibit 41. I ask you if that, or any part of that is in your handwriting?

A Yes.

I looked at this this morning. This is my handwriting. This is the receipt I gave to Mr. Silverman, I believe.

Q Sir, I show you this document marked as plaintiff's exhibit 36 and ask you if you've ever seen that before?

A No.

Q Have you ever seen a copy of that before?

A Yes. I've seen it this morning.

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Shevack-direct

Q Where, sir?

A In your office.

Q Sir, it has been testified by both Mr. and Mrs.Silverman, that you prepared that document known as a W-2 form and handed it to them.

Was their statement true or false?

A False.

Q Sir, did you ever have a conversation with Mrs. Silverman, or with anyone else, at which time you were provided with the social security number of Mrs. Silverman?

A Of Mrs. Silverman?

MR. LERNER: Objection, your Honor.

Q Yes.

A No.

MR. GOIDEl: What's the objection?

MR. LERNER: Calling for hearsay answer.

THE COURT: Let me hear it back.

MR. GOIDEL: I'll rephrase it differently, your Honor.

THE COURT: Let me hear what was said.

Q Sir, there is a -- what purports to be a social security number on plaintiff's exhibit 36. That number purports to be 063-38-0248.

7

Sir, did you ever hear of or see that number before you were in my office today?

A No, I did not.

Q Now, sir, Mr. and Mrs. Silverman claim that on two different days you drove them to approximately 6 financial institutions with a view towards them borrowing monies.

Sir, did you, at any time, drive them to any one or more lending institutions, banks, financial institutions or any other type of lending institution?

A No, I did not.

Q Sir, you understand you're under oath?

A Yes, I do.

Q You understand that if you lie, you are subject to the penalties of perjury?

A Yes, I do.

Q Any of the other individuals whom you sponsored into Galaxy -- I'm sorry -- withdraw that.

Did you advise any of the other people whom you sponsored into Galaxy, those are people other than the ones I have just named, did you advise any of them to borrow money, to make out applications, to take out loans, in order to obtain the funds necessary to purchase a franchise?

A No.

Getting the money was their problem.

Q Did you ever answer any questions from any individuals?

A Sure, I did. I answered questions.

Q Would you give us an example? Would you tell us the time, the date, the place or an individual with whom you had such discussions?

A Well, most people have money, but they don't tell you. Everybody is broke. Nobody can afford nothing.

But when they're on the line and they have to get it and they want to get it bad enough, you'd be surprised. They find a way to get it.

So, you know, many people, they'd alway ask me for a loan. I tell them, I says, "Nobody lent me the money. You want the money" I says, "look in the newspaper, go wherever you got to go, to your friends, neighbors, get $10 from a thousand people. Do whatever you got to do. You want it, here it is."

Q In fact, sir, in a way you did borrow the money yourself; did you not?

A I borrowed the money myself? I didn't really borrow it. I earned it.

Q Okay.

9

Shevack-direct

A If they wanted to earn it, that opportunity was there for them.

Q Sir, did you ever hear of A&M Dental Lab?

A No.

Q Sir, was Galaxy your first venture into franchise sales?

A No, it was not.

Q Had you earlier been associated with any firm related to the franchise industry or business?

A Yes, I was.

Q Would you tell us what your first association was of that type?

A That was Koscot.

Q The famous Koscot International?

A Infamous.

MR. GARMANSKY: Objection, your Honor. That's not the name.

THE COURT: What is the name?

MR. GARMANSKY: It's not the name Mr. Goidel said.

MS. MYSLIEWIEC: Koscot Interplanetary Incorporated.

THE WITNESS: Koscot Interplanetary Incorporated.

10

Q Would you tell us what your association was with Koscot?

A I had purchased a distributorship from them.

Q How did you purchase that distributorship?

A Out of my pocket.

Q How much did you spend out of pocket to purchase that distributorship?

A I gave them certified checks totalling $5,000, out of my personal account.

(continued next page.)

11

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Shevack-direct

Q Did you have any other association with Koscot other than as a distributor?

A Later on, toward the end of my time with them, I was an assistant state director, I think, Brooklyn, I forget.

Q What was an assistant state director?

A In charge of maintenance, basically. It was --

Q Maintenance of what?

A If there is a -- a meeting room needed, it's your responsibility to go over and make sure it's arranged, the blackboard is there, the chairs are there, the place is clean. You know, that type of thing.

I would try to make sure some loose ends were tied up when they were going to have a meeting or something like that.

Q Were you paid monies on account of those services?

A Yes.

Q How much were you paid on account of those services?

A The largest check I ever received, and we were paid monthly, was approximately a little more than $400 for the entire month.

Q Sir, you say that you had a distributorship.

12

Did you earn monies through the distributorship?

A Yes.

Q Would you tell me how your distributorship functioned, what it did, where it did it and how it was done?

A Well, I incorporated that distributorship with some other products and I opened a store.

Q Where did you have your store?

A That was at 1502 86th Street in Brooklyn. I also --

Q I'm sorry, go ahead.

A There were many other locations that I had also. 193 Waterman Avenue in Providence, Rhode Island.

Q All at the same time?

A Yes.

I had quite a few locations and we were selling various products, Koscot's products and many other types of products also.

Q What type of products were you selling?

A We were selling cosmetics. We were selling jewelry. We were selling perfumes. We would sell clothing. We would sell hairsprays.

Anything, you know, you could turn over and make a profit on.

13

Shevack-direct

Q Who paid the rent for your stores?

A We did, or I did.

Q Now, were you an officer of Koscot?

A No.

Q Shareholder of Koscot?

A No.

Q Director of Koscot?

A No.

Q Did you serve that corporation in any other capacity, other than as you described it, an assistant director, or something, of Brooklyn?

A No.

Q Your only other relationship with that firm was as an independent retailer franchise owner; is that correct?

A Right.

Q Did you ever sell your franchise back to Koscot?

A No.

Q Did you ever sell your franchise that you paid $5,000 for to anyone?

A No.

Q Do you still own that franchise?

A Yes.

14

Shevack-direct

Q Sir, did you have any other prior association with any franchise operations other than that original association that you have mentioned now with Koscot?

A No, I do not.

Q Now, sir, what is your present vocation, present position, present job?

A Presently I'm vice-president of the Futuristic Foods, Incorporated, Rego Park Corporation, organized under the State laws of New York.

Q What is the business of Futuristic Foods?

A We sell food to consumers who wish to have their merchandise delivered.

Q Do you also sell franchises?

A Yes.

Q Now, sir, at the present time do you sell franchises to give to the others the right, in turn, to sell franchises and earn a commission?

A No.

Q Did you, at any time, sir, sell to anyone, franchises which in turn, gave them the right to sell a franchise and earn a commission?

A Yes.

Q Can you tell us, sir, when and under what circumstances, Futuristic Foods stopped selling franchises

15

which carried with it the right to sell franchises and earn commission?

A We were advised by yourself that on August 23rd, any franchises sold at that point, the commissions earned by those people were to be given to you and placed in escrow. At this time, --

Q I'm sorry, go ahead.

A At this time there is $8500 that's been placed in escrow, which was the agreement, I believe you said we had with the court.

Q That was the instruction of his Honor, Judge Connor?

A Yes.

Q Is that correct, sir?

A That's correct.

And should I elaborate?

Q Does Futuristic Foods sell food?

A Yes, it does.

Q Does Futuristic Foods pay a commission on the sale of that food?

A Yes, it does.

Q Does the commission on the sale of the food that had been paid to day -- withdraw that.

Do you know how much money has been paid as

16

commission on the sale of foods by Futuristic Food?

A The exact specifics would be difficult. I could get them; but I know it's in excess -- it's thousands and thousands of dollars that we've paid the franchisees ever since the first day we delivered our first, you know, steak.

Q When was the day on which you delivered your first steak, if you know?

A December 6, 1973, our first trucks rolled.

Q How many trucks do you presently have?

A Well, we own 5. We lease 5. And take a day like today, we're renting an additional 3 to 4 trucks because, you know, we just don't have enough to get them out.

Q Now, did there ever come a time that you had discussions with anyone in Galaxy as relates to the propriety or legality or illegality of anything being done in or through that corporation?

A Yes, there were a few occasions.

Q Can you tell us approximately when you first made inquiry, and the circumstances under which such inquiry was made?

A September, you know, vaguely.

Q Of what year?

17

Shevack-direct

A Of '72.

Q Could you tell us of whom you made the inquiry and the circumstances under which it was made?

A Well, I was speaking to Mr. Lieberman in his --

Q By "Lieberman" are you referring to the same person that you previously referred to before as "Lee"?

A Yes. It's one and the same.

We were in his corporate office in the warehouse and I had gone in there for a moment and he didn't seem too busy, and it seemed like I could talk to him, and I started our conversation as to, like, you know, what's going on, is everything all right, how are things going, you know, we're getting bad reports here, and some of my guests are not satisfied with the type of information they're accumulating on the corporation and, you know -- and he said, you know, "I've spoken to my attorneys."

Q Did he tell you who they were? Who the attorneys were?

A He did. Rothstein, Rothschild. He did. I really -- I don't recall the name. If I heard it, I'd remember it.

But he was discussing it, you know, and he said, "The attorneys are working on it." He says, "No problem, don't worry about it, keep the faith, do what

18

Shevack-direct

you're doing." You know, no problem.

That was the general question we got.

Q What made you make this inquiry, sir?

A Well, you know, the date that we were supposed to start delivering food, you know, to start accumulating some of these commissions, was postponed once and twice and then three times, and I could see that things weren't functioning the way I'd like to have seen them function.

I know my income was limited. There was only one way to earn money at that point, to sell franchises, which is a very difficult thing to do. And it's much simpler, you know, to just get someone to purchase food and to sit back, and, you know, live off the overrides you can earn from them just ordering. You don't have to sell them food perpetually, but there is a very heavy push, you know, all the time, to find new business.

So I was hoping to take it a little bit easier, hoping for the food operation to get started, and when it finally did start, we weren't going to be entitled to receive any money on that either.

So that's what kind of, you know, climaxed the whole thing and we just decided to leave.

MR. GOIDEL: Your Honor, do you wish me to start a new line?

THE COURT: No. Let's break now.

Can we make it back at 2 o'clock, do you think?

MR. GOIDEL: Your Honor, I hope to be finished within 30, 35 minutes. Thereabouts, after.

THE COURT: So you are suggesting we make it 2:15? Is that it?

MR. GOIDEL: No. I'm just saying it so that the Securities and Exchange Commission will have a better idea as to when they can anticipate starting cross examination.

THE COURT: Can we resume at 2? Any problems?

MR. GARMANSKY: No, your Honor.

THE COURT: All right. Let's adjourn until 2 o'clock.

(Luncheon recess taken.)

mMPhb

AFTERNOON SESSION

ARTHUR SHEVACK, resumed and testified further as follows:

DIRECT EXAMINATION

BY MR. GOIDEL (Continued):

Q Mr. Shevack, were you instructed as to any limitation relative as to whom and where you could sell or endeavor to obtain an application for the purchase of a franchise?

MR. LERNER: Instructed by whom?

Q Anyone associated with Galaxy Foods.

A Yes. We were instructed that only a resident of New York State may purchase, he must be at least -- he or she must be at least 21 years of age and we should use personal contact in order to endeavor to sell or find people to buy.

Q Sir, did you ever endeavor to sell a franchise to anyone not a resident of the state?

A No.

Q Now, sir, did you and Mr. Silverman ever have a quarrel?

A Yes, we did.

Q Will you describe where, when, and the circumstances around which this quarrel occurred.

A I believe this was around December.

Q What year?

A 1972. I was in the Broadway area near Pine Street or Wall Street, that section, on one of the side streets and I met Mr. Silverman. He was coming in the opposite direction on the same side of the street. When he noticed it was me approaching he quickly approached me and seemed to be a little frantic upon his approach.

Q Frantic about what?

A When we finally got close enough to start talking he was talking extremely loud and seemed very aggravated that number one he was losing his money in Galaxy Foods or had lost his money in Galaxy Foods, and I told him to join the company -- this is what he was saying -- and then he went off on another tangent. He started yelling and screaming at me that he has been hearing that my brother was fooling around with Georgette. Georgette was his wife.

Q What did you say to him about either or both of those items?

A I told him I was under the assumption at the time that Galaxy Foods -- there was nothing wrong with it and he was really, I don't know if he was coherent, I don't know the exact word but he was a little strange upon speaking to him.

MR. LERNER: Your Honor, I have to object to

this line of testimony. Mr. Shevack is relating a hearsay tale between himself and a person who is not in court.

THE COURT: I am not so sure about that. I thought he was relating a conversation that took place between he and Mr. Silverman. He testified here. And of course the credibility, bias, hostility and other aspects might be in issue.

Now, of course it is open to the Commission to recall Mr. Silverman as you know, upon issues like that.

Q What if anything, sir, was said with regard -- by you, with regard to the accusation concerning or involving your brother?

A I explained to him that I hadn't seen my brother at that time for over a year and whoever told him the story was not too bright. He was just trying to create some animosity. Whoever told him, might have known me. And Steve was very upset. And I have heard various rumors also.

Q Did you mention to him that you heard rumors?

A Yes, I explained after he had the situation it was his problem and not mine and he shouldn't try to tell me. I told him to watch his wife closely. In fact, there were many rumors that had been circulated. In fact, Terry

Varano who was her associate in the same hospital, another nurse, used to tell me some of the stories --

MR. LERNER: Objection.

MR. GOIDEL: O.K.

Q Just tell me, sir, what you said, not what Miss Varano said or anyone else? Is that the extent of what you said concerning this?

A I tried to limit the conversation as much as I could. I was getting nowhere speaking to him. It was like talking to a wall. I couldn't talk over him and he wouldn't take a breath. He yelled and I yelled and I said, "Think what you want," and I left.

Q Did you have any other source of earnings while you were associated with Galaxy Foods?

A No, not at all.

Q Was this your sole vocation?

A Yes.

Q Sir, when you entered by purchasing a franchise, do you know approximately how many franchises there were left to be sold?

A (No response.)

Q To put it another way, do you know what number you were as a franchisee?

A Approximately, I believe my number was around

400.

Q Were you aware of the fact that there was a limitation on the total number of franchises that could be sold?

A Yes, I believe the number was 1,079.

Q Sir, did you set up an organization to retail food?

A Yes.

Q Now, sir, was it your intention or was it not your intention, upon the completion of the sale of franchises to continue in the operation of selling food?

MR. LERNER: Objection, your Honor. That calls for a conclusion and it is also a hypothetical question. It is also immaterial.

THE COURT: First of all, let's find out -- I will sustain the objection. When was this organization to retail food?

Q When did you set up an organization to sell food retail?

A I actually started setting up -- I would say around October, November. Really started getting into it.

MR. LERNER: What year?

Q What year?

A 1972. Everything is 1972.

Q What did you do?

A Well, I was speaking to people as far back as September about using the service and around that time, even a little before that they were explaining shortly they were going to start delivering food. They kept postponing the time they were actually going to start. But it seems -- the general feeling was it was going to start around the October area.

Q What did you physically do in order to promote the sale of food?

A We started knocking on doors.

Q Who is we?

A Myself, Mr. Kinsella, I had a couple of relatives of mine referring people who wanted to use the food service to me. I would see people I met, contact many of the guests who I brought down who did not want to purchase a distributorship. I called them and asked them if they would like to use the service and told them we are now going to start delivering food. And not even discussing the franchise operation, just talking about: Do you want to be a customer.

Q Now, sir, did you have any other expenses other than the expenses which you have already described for us?

A Like what? Gas? I don't understand.

Q Did you purchase anything specifically in connection with your work, your business?

A Purchase anything? Nothing really major.

Q Leaflets, anything of that sort?

A Business cards I purchased, flyers, I printed up material, advertising that I printed up and handed out. That type of thing, sure.

Q Did the corporation pay you for that or did you?

A I paid for that.

MR. GOIDEL: Your Honor, I have no further questions.

THE COURT: All right.

CROSS-EXAMINATION

BY MR. GARMANSKY:

MR. GARMANSKY: May we have two minutes?

THE COURT: You may.

(Pause.)

Q Now, Mr. Shevack, you testified that you first heard of Galaxy in June of 1972, is that correct?

A Approximately, yes.

Q Now, please tell us once more how you came to hear about Galaxy in June of 1972?

A I was at the Chameleon Room, a catering hall on Avenue U. I went down there and I walked in and spoke to

the owner and Artie Lee was there in the hall. We first met each other --and he said hello and I said hello. I recognized one or two of the other individuals although I don't recall now who it was, and he explained to me basically what he was doing at the time. He said he was the Chairman of the Board of the corporation and I was friendly with him going back maybe a year before that. So he invited me in. He said, "Sit through it."

I was curious and went into the Opportunity meeting. That's when it was and where it was held. That was about it. After that we went for coffee.

Q Mr. Shevack, do you remember appearing before the Securities & Exchange Commission on or about December 17, 1973 to give testimony?

A Yes. I don't recall the exact date but I guess that is it.

Q Were you represented by counsel?

A Yes.

Q Who was your counsel?

A Mr. Goidel.

Q Do you recall being placed under oath before and asked questions?

A Yes, sir.

Q Do you recall being asked a series of questions

and you giving answers to those questions?

A Yes.

Q I am going to read to you some questions and answers, tell me if you recall these questions and you giving these answers.

THE COURT: Are you going to do it on a one-to-one basis?

MR. GARMANSKY: Yes, your Honor. Page 14, line 6.

Q "Question: Mr. Shevack, have you ever heard of a company called Galaxy Foods?

"Answer: Yes, I did.

"Question: When for the first time?

"Answer: I can't exactly remember the date it was about --

"Question: Not exactly, approximately.

"Answer: A year and a half ago, I guess.

"Question: Would you place the month?

"Answer: I honestly don't recall the month.

"Question: A year and a half ago? Approximately April of 1972?

"Answer: Let me recall. That was possibly correct, O.K.

"Question: April '72?

"Answer: Right."

Do you recall those questions and do you recall giving those answers?

A Yes.

Q Which is it, June or April of '72?

A As I stated there, I wasn't sure of the exact time.

Q Not what it says here --

MR. GOIDEL: Just a moment.

THE COURT: You can't argue with the witness, listen to the explanation if he has one.

A As I stated there I didn't recall exactly when. I was assuming he knew more than I did about the dates. I didn't have any information as to exactly when it was at my disposal.

Now, I checked the date since that time precisely and I spoke to Mr. Lieberman and discussed it with other people here. And I feel at this point June is a more correct answer to that question than I have given you previously to the best of my recollection. I am still not exactly sure.

Q Mr. Shevack, you testified that you received a phone call from Mr. Lieberman approximately a year before you heard about Galaxy, is that correct?

A A year before I heard, yes.

Q How did you know the phone call was from Mr. Lieberman?

A I was familiar with his voice.

Q You talked to him?

A Sure.

Q In your direct testimony you said you never returned the call, isn't that correct?

A When I said I never returned the call, what I meant by that was I wasn't responding to the conversation. He was coming across to me on the phone inviting me to an opportunity meeting to join the corporation, which I didn't want to do at that time. I didn't feel it had any value to me or that I could benefit from it.

Q Mr. Lieberman invited you to a meeting at this telephone conversation?

A Not a meeting, just a get-together.

Q You testified on direct you did not return the phone call, was a call supposed to be returned?

A I was supposed to call him back. I did not.

Q Now, Mr. Shevack, what did Mr. Lieberman tell you in that phone call about Galaxy?

A It was very brief. He told me that he was starting a food company and it is something good. He said, "You won't get hurt like you got hurt in Koskot." He said to

come down, it was something good. He said, "You have ability, initiative, this is the type of thing that would be good for you. Come down and take a look."

I wanted no part so I refused.

Q This phone call was about June 71, is that correct?

A Yes.

Q Now, Mr. Shevack, you described that Mr. Lieberman told you on the phone that you wouldn't get hurt like you did in Koskot?

A Yes.

Q Were you hurt in Koskot?

A At the time I didn't think I was but later on I found I was.

Q How did you find out?

A The company went bankrupt.

Q Did you make money?

A Some. I also spent.

Q Did you earn more than you spent?

A No.

Q You didn't?

A No.

Q How were you paid in Koskot?

A On commission.

Q On commission from people you brought in?

A Yes.

(Continued on next page.)

Q That was the only way you were paid in Koscot?

A Also I was Assistant State Director.

Q Did you get paid?

A The biggest check I ever got was for $400 a month.

Q Tell me how you got paid for being the Assistant State Director.

A I received, I think it was either one quarter or one half a percent of the area I was in.

Q I don't understand your answer. How can you get one quarter or one half of a percent of the area you were in? What did you have to do?

A This would depend on the distributors in that area.

Q An override on everybody else that you brought in, is that correct?

Only in a specific area.

Q You would get that override on everything else brought in and joined Koscot in that area?

A Yes.

Q So you made money in the override and money from selling franchises yourself, is that correct?

A If you decide $400 a month was money, yes, I made money.

Q Now, you testified as to the functions as Assistant State Director, is that correct?

A Yes.

Q Would you please go over them once more.

A We were in charge of getting rooms, halls or whatever the case may be. Making sure that loose ends were tied up. Everything was ready to go for the opportunity meetings. Let me see what else.

Oh, projectors, films, things like that. That is, if there was a film that was available.

Q This is all you did as Assistant State Director?

A Not all, there are a couple of duties. It's hard to recall what my duties consisted of.

Q What is your best recollection?

A Designate speakers to speak at meetings, and that is about it.

Q For this you got paid half a percent a month?

A Half or one quarter, I don't remember exactly.

Q I want to correct my question, you got paid a quarter to a half percent on all people that were brought in in your area?

A Yes.

Q Total gross sales --

THE COURT: When you use the expression 400 a

month, what do you mean?

THE WITNESS: Four hundred --

THE COURT: During one month period?

THE WITNESS: Four weeks.

THE COURT: Are you saying that there were no more months in which you were paid anything?

THE WITNESS: Yes, there were months I got zero. They didn't give me a dime. I worked for nothing.

THE COURT: Over how many months did this connection extend?

THE WITNESS: Ten months. Within that ten-month period I venture to say I never received more than $1100.

THE COURT: Over all?

THE WITNESS: Over all.

THE COURT: That would include the 400 you mentioned?

THE WITNESS: Yes.

Q You had a discussion with Mr. Lieberman in Brooklyn at Koscot?

A Yes.

Q What did you and he talk about?

A His company.

Q You mentioned on direct that Mr. Lieberman told

you Galaxy could fit you like a glove?

A Yes.

Q Isn't it a fact Mr. Lieberman said that because of your prior association in Koscot, you were going to do the same selling method?

A I don't know what he meant by it, it's possible.

Q How many meetings did you attend before you officially joined Galaxy by signing the contract?

A It is very hard to say, approximately 15. I really don't know exactly.

Q Is that your best recollection, Mr. Shevack?

A Yes, my best recollection.

Q And you joined Galaxy officially in July of '72, is that correct?

A Yes.

Q How many meetings did you attend, both opportunity and Sunday Step-Up meetings after you joined Galaxy in mid-July of 1972?

A Numerous. I attended most of them I would say.

Q How many would that be?

A From July to December -- 50, a hundred. I am giving you ball park figures.

Q Anywhere from 50 to 100?

A Yes, something like that.

Q When did you terminate your association with Galaxy?

A I stopped working in June but I terminated I believe the end of December or beginning of December of '72. I actually sold my franchise.

THE COURT: In June?

THE WITNESS: December of '72. I found a buyer to purchase it and I sold it.

Q I would lke to show you this document, Mr. Shevack Can you tell me if you recognize it?

A Yes, I recognize it.

Q What is it?

A I believe this is when I gave testimony --

By the Securities & Exchange Commission?

Q No, Mr. Shevack. Look at it closely. Isn't it your affidavit, Mr. Shevack, that you filed in this action?

A I assume so.

Q Look at the document, Mr. Shevack, and tell me if you have ever seen it before.

MR. GOIDEL: Your Honor, Mr. Garmansky has a way of being a little overbearing with the witness. I appreciate that this is cross-examination, but he already asked him to look it over carefully. Let's let him.

MR. GARMANSKY: That's what I want him to do, Mr. Goidel.

MR. GOIDEL: O.K.

(Pause.)

A Yes, I looked it over.

(Continued on next page.)

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Q Do you recognize the document?

A Yes, I do. I don't know what name you legally give this document, but I recognize it.

Q It's an affidavit?

A OK.

Q Is that your affidavit, Mr. Shevack?

A Yes.

Q Did you sign that affidavit?

MR. GOIDEL: We'll stipulate that the original is on file with this Court, if that's the affidavit which was part of this proceeding.

Q You signed the original affidavit; did you not?

THE COURT: Do you want to find the original in the file?

MR. GARMANSKY: Is this it?

THE COURT: Everything is there that is there. What is the date?

MR. GARMANSKY: The date here, it says third day of November, '73, which is obviously wrong. The case wasn't filed until the 26th of November. I think it's the 30th.

THE COURT: The 30th?

MR. GARMANSKY: Probably be the 30th of November.

THE COURT: It might be attached to a motion paper.

MR. GOIDEL: Show it to me and I'll give you a stipulation.

MR. LERNER: Stipulate to it.

MR. GARMANSKY: Your Honor, counsel for Mr. Shevack will stipulate with the Commission that it is the affidavit Mr. Shevack signed and he filed with this Court.

THE COURT: All right.

BY MR. GARMANSKY:

Q Now Mr. Shevack, when you signed this affidavit, did you realize that you were swearing to the statements made in this affidavit as to their truth and accuracy?

A Yes.

THE COURT: It is found.

MR. GARMANSKY: I think this is it.

THE COURT: Is it or isn't it?

MR. GARMANSKY: Yes, it is the same one.

I see, though, under the notary it has the third day of November, 1973. It looks -- appears to be the third day.

MR. GOIDEL: The difficulty must mean it is my handwriting.

Q I show you the original now, Mr. Shevack, of the copy I had previously shown you. Would you please direct your attention to Paragraph Six of your affidavit?

A Yes. This is Mr. Kirschenblatt's affidavit, if you want to be technical.

Q We'll have to find yours.

A I don't know where it is.

THE COURT: Is there more than one? More than one attached?

Q This is yours. I direct your attention to Paragraph Six on Page 2. It states, "In October, 1972, I disassociated myself from the corporation by disposing of the franchise which I had purchased."

Mr. Shevack, you've just testified it was in December where you disposed of your franchise in Galaxy Foods?

A Yes.

Q Your affidavit says you disposed of your franchise in October of '72. Which one is correct? Your testimony or your affidavit?

A Well, honestly speaking, I was unsure of the dates and I was trying to be as precise as I possibly could be.

I felt at that time that October was the proper date, and the only reason I'm trying to clarify it is that at this point I understand that I sold my franchise in December

and not October, as I previously believed I did.

Q Well, when you signed your affidavit some time in November, 1973, until today, what caused you to change your mind?

A Well, from speaking with other individuals and Mr. Padilla. He told me that in October I did not sell my franchise. I sold my franchise in December. And it was his mother who bought it. So it's possible -- it's very possible that he's more familiar with the date than I am.

Q So in other words, your affidavit is not correct?

MR. GOIDEL: Objection, your Honor. He has already explained the distinction between the October and the December dates.

A (continuing) You see, my attorney and myself, after appearing before you, we were unsure about many things and we had sent a letter to Galaxy Foods, asking them for specifics, dates on who I brought in and how many people there were. We were unaware.

I don't believe as yet we've received an answer to that letter, to this date.

I don't have any records. I discarded them when I disposed of the franchise, and the exact dates I don't know. I just don't remember the exact dates.

Q Do you recall when in December you left Galaxy,

Mr. Shevack?

A No.

Q Early December, late December?

A I just hope it was December.

Q Well, we're assuming you're telling the truth now, Mr. Shevack, so we're going to go on December of '72 as the date you left Galaxy.

A Yes.

Q Is it early December or was it late December?

A Early December.

Q Early December. OK.

A I was up all last night looking for the --

Q Just answer my questions, please, Mr. Shevack.

Now, Mr. Shevack, approximately how many customers did you acquire for the retail food service of Galaxy?

A That actually purchased food?

Q No. How many did you acquire who were ready, willing and able to purchase food?

A Personally or through everybody's efforts?

Q Your whole organization, Mr. Shevack, because you were the head of it; weren't you?

A Yes.

Q How many did you acquire?

A I'd say, with everything combined, about two

hundred, give or take a few.

It's hard. It's hard to recall.

Q That's your best recollection; isn't it?

A Yes.

Q How many people out of those two hundred did order food and received food?

A I don't know.

Q Approximately, Mr. Shevack?

A Fifty.

Q About fifty. And did you receive any commissions?

A No.

I didn't even get a statement that they got a delivery.

Q Do you know whether or not these people did get food delivered?

A No. I spot-checked a couple, but other than that, no.

Q Well, did the people you spot-checked, did they receive their food?

A Some of them, yes.

Q Some of them did?

A Some did and some didn't.

Q Did you get these orders from these fifty some-odd people and give them in to Galaxy?

A Yes.

Q Now, the people who didn't get their food, did you do anything?

A The corporation was telling us that there is nothing that they could do at this point. They didn't have a computer system. They didn't have the personnel on hand to do everything proper.

Q Did you do anything about that?

A There was nothing I could do.

Q Did you explain this to your customers who didn't get the food, even though they ordered it?

A The customers were yelling at me. The few that I'd call were annoyed at that point.

Q But at least a few of your customers did get food delivered; that's correct, isn't it?

A I believe so.

THE COURT: When were the customers to pay for the food, upon delivery?

THE WITNESS: Yes, upon delivery. They were supposed to pay the driver.

THE COURT: I see.

BY MR. GARMANSKY:

Q Now I'd like to read you some questions and answers again from your transcript of approximately September 17, 1973, and tell me if those answers -- you heard those

answers -- those questions being asked and those following answers being given. This is Page 56, Line 5.

"Question: Did you obtain any customers, Mr. Shevack, for the home delivery food service by Galaxy?

"Answer: I had many customers, but they were not paying commissions on any customers of quantity.

"Question: But you did have customers who were ready and willing to order food from Galaxy?

"Answer: Oh, yes.

"Question: About how many?

"Answer: A couple of hundred.

"Question: Were they in the delivery zone area from the warehouse?

"Answer: No, they were not.

"Question: None of them were?

"Answer: I didn't live in that particular area."

Do you recall those questions, Mr. Shevack, and do you recall giving those answers?

A Yes, I did.

Q Mr. Shevack, in your transcript you've stated that none of your customers had food delivered to them. Right now you are saying that some of them did.

MR. GOIDEL: Objection, your Honor. I don't know that that's what the testimony says.

You've asked a question and you read back the answers. If you have any question about its meaning, ask the witness.

BY MR. GARMANSKY:

Q OK, Mr. Shevack. What did you mean when you answered this question:

"Question: Were they in the delivery zone area from the warehouse?

"Answer: No, they were not.

"Question: None of them were?

"Answer: I didn't live in that particular area."

What did you mean by those answers, Mr. Shevack?

A Well, there were so many who weren't in the area that, you know, the very few who might have been, you know, seemed, you know, almost insignificant in comparison.

Q So you didn't want to tell me about those few on the day you testified?

MR. GOIDEL: Objection; argumentative.

A (continuing) At that time we were, you know, discussing Galaxy Foods, but, you know, I was so annoyed with them. They were a little annoyed with me, and whatever the case was, but honestly speaking, there were a couple of customers who might have got delivery, who did live closer to the plant location.

2pm2 gr/nc

CROSS-EXAMINATION

BY MR.GARMANSKY: (Cnt.)

Q Mr. Shevack, when you solicted these customers, did you tell them they were not in the delivery area?

A At first, we didn't know where the delivery area was. It changed on a daily basis.

Q Mr. Shevack, whendid you find out that the majority of your customers were not in the delivery area?

A About the same time they were starting to tell us that they weren't going to pay com missions.

Q When was that?

A The best of my recollection, December, November, you know, that type of area. Toward the latter part of my stay with Galaxy.

Q November or December; is that correct?

A I'd say November, I think maybe a little more than December.

Q November, a little more than December?

A Yes.

Q What did you tell these people?

A Which? The customers?

Q Yes.

A I told them that they were either going to have to wait until, you know, the delivery area would be

expanded to their particular location or until we got enough customers from a particular area to accept the delivery and then talk to Galaxy about sending a special truck because the volume was good, they'd go -- out of their area, if you could substantiate -- excuse me, a concentrated area where they could send one truck to do everything.

Q How did you tell these customers this? Did you call them up? Did you write to them? How did you tell them?

A Many of them I went back to see. Just the same areas, knocking on doors, telling people, you know, you want to use the service, when would you like to use it? These are products that we're going to carry now. Any suggestions? Trying to become a little friendly.

Q But you went back to all your customers?

A No, not all the customers. Many I forgot about. I just got disgusted with.

Q How many did you go back to to tell them that you're not in the delivery area?

A The ones I knew I guess a little better than others.

Q How many?

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A Ten.

Q Ten?

A Yes.

Q Out of 200?

A Yes.

Q That's all you've told was ten?

MR. GOIDEL: Objection, this is going a little too far.

THE COURT: Mr. Garmansky, you have to restrain yourself.

MR. GARMANSKY: Sorry.

THE COURT: Argument comes at the end of the case and not while you're questioning a witness.

MR. GARMANSKY: I'm sorry, your Honor.

THE WITNESS: I saw no point to it.

BY MR. GARMANSKY:

Q Now, Mr. Shevack,did you ever physically go out to obtain some of these customers?

A Yes.

Q How many customers did you personally obtain, that were ready and willing to use the food delivery service of Galaxy?

A Maybe 50. By myself.

Q Okay.

While you were doing that, Mr. Shevack, did you also ask them if they would like to buy the franchise?

A No.

Q None of them you did that with?

A No, none.

Q You're certain of that?

A I'm pretty certain of it. I don't think I discussed franchises with them. I think I discussed, you know, just the customers with them. Just food order.

Q Just the order food?

A Yes.

Q You didn't happen to say, by the way, Galaxy has some more franchises they can still sell and would you be interested in joining the Galaxy association?

A I can't honestly say it never happened. It might have happened. Customers were very curious about the service. It was new. It was unique.

Q Now, you paid $5000 for your franchise? Is that correct?

A Yes.

Q And you became associated with Mr. Lieberman's organization; is that correct?

A Meaning, Galaxy Foods?

Q Yes. But his own distributorship

association, his own organization?

A Vaguely.

Q Okay.

Were you working for Mr.Lieberman?

A Yes. I would say that was more in line with it.

Q Okay. And you were going to sponsor people into Galaxy and you would get the commissions; is that correct?

A Well, I would bring people down. If they wanted to buy, he'd have to sign them up and then he'd give me the commission.

Q Exactly.

A Right.

Q Now, did you receive any money from Mr. Lieberman or was the money left in Galaxy on your behalf towards the purchase of a distributorship?

A No. He gave me the money.

Q He gave you the money?

A Yes. Physically. In my pocket.

Q Did you have to go to Sunday Stepup Meetings to get the money?

A Most of the time, yes.

Q You did?

A Yes.

Q So in other words, you were not a distributor in Galaxy but you went to the Sunday Step-up Meetings to receive your checks?

A No, I never got a check. I never got a check. He would give me cash or his own personal check and he never gave me a Galaxy Foods check.

Q He gave you cash? In other words, over a period of time, about a month and a half, he gave you $5000?

A Yes.

MR. GOIDEL: Objection. Your Honor --

THE WITNESS: Wait, can I clarify?

MR. GOIDEL: Please. When I make an objection, you keep quiet.

THE COURT: All right.

MR. GOIDEL: The witness said cash or personal check. You've abbreviated again to cash. That was not his statement.

MR. GARMANSKY: Okay.

BY MR. GARMANSKY:

Q In other words, from June when you became associated with Mr. Lieberman's organization, until mid July when you joined, you received $5000 from Mr.Lieberman

in cash and checks?

A Yes. He never made a Galaxy Food check out with my name as the payee.

Q I see.

How much did you get in cash from Mr. Lieberman?

A Almost -- about -- now I'm trying to break it up into cash or check. I don't recall. I remember I got approximately $5000 in different denominations of different things.

As I was productive, he would pay me whatever I was entitled to.

Q Different denominations of different things? Only two type of things you could get; cash or check?

A Gave me hundred dollar bills, twenty dollar bills, fifty dollar bills. Different denominations of cash and checks.

Q Okay.

Now, my question is very simple, Mr. Schevack.

Do you recall how much cash you were given?

A Specifically cash as opposed to check?

Q Yes. That's correct.

A No.

Q You don't? Do you recall how much money you received in checks from Mr. Lieberman?

A No, Do not.

Q Now, did you receive your cash and your checks at Sunday Step-up Meetings?

A Most of the time. Not all the time. Because he was there on Sunday and usually he's very hard to find.

Q Well, did you?

A He owed me money.

Q Was your name called out and did you have to go up in front of the guests and the existing investors in Galaxy to receive the cash or checks?

A No, I did not.

Q I see.

A It was off the record.

I wasn't in Galaxy Foods.

Q I see.

And you took this $5000 and you bought a distributorship?

A Yes.

Q Whom did you pay the money to?

A Arty Lee.

Q How did you pay him?

A It's possible I gave him a personal check for a portion of it and some cash for the balance.

Q Is that your best recollection, Mr. Shevack?

A That's my best recollection at this point. I could check my check stubs and find out whether or not I did give him the check but I think I did.

I wanted a receipt, I remember that.

Q Now --

THE COURT: I want -- when you made this payment was it $5000?

THE WITNESS: YEs. I had to add to it.

THE COURT: All right.

But I mean, it was 5000?

THE WITNESS: Yes. Not a penny less.

THE COURT: Do I understand that you made -- if you did make a check, and I take it perhaps some part of it was made by check; is that what your testimony is?

THE WITNESS: Yes. I might have given him a check for $2500 and gave him cash for $2500. You see--

THE COURT: My question really is, when you made out the check, was the check made out to Galaxy Foods or not?

THE WITNESS: It was made out to Galaxy Foods, Inc..

BY MR. GARMANSKY:

Q Now, Mr. Shevack, how much of the $5000 did you

earn before you signed your contract with Galaxy? 5,000 Mr. Lieberman paid you. How much did you earn of it?

A All of it.

Q Now, how much money did you earn in Galaxy after you signed your contract in mid-July, 1972?

A Approximately $11,000.

Q And you earned $11,000 from mid-July until you left Galaxy; is that correct?

A Yes.

Q So that altogether, Mr. Shevack, you earned approximately $16,000 with Galaxy Foods even though Galaxy did not pay you the five, you still earned it; is that correct?

A Working for Mr. Lieberman.

Q Okay.

But you still earned it?

A All right. But I had two separate jobs.

Q Fine.

You eanred 11,000 with Galaxy. That's approximately $16,000.

A When you say with Galaxy, I wasn't with Galaxy.

Q You earned 11,000 with Galaxy?

A I'm sorry, yes.

Q That's about $16,000.

Now, Mr. Shevack, I'm going to show you a series of checks from Galaxy Foods, Inc., made payable to yourself. I want you to tell me if you received the money for all of these checks?

A I can't tell you that.

Q Why can't you tell me that, Mr. Shevack?

A There is no stubs.

Q There appear to be endorsements on the back.

A But it is very possible that the check was cashed and given back to Galaxy Foods.

Q Do you recall? Just look through the checks, Mr. Shevack.

A Here. For instance, pay to Galaxy Foods is on the back of this check and I signed it. Pay to Galaxy Foods is on the back of this check and I signed it.

That's their bank stamp, Galaxy Foods. They redeposited these. I can't tell without the stubs. I don't know why they were given to me. All it is is a check, pay to Galaxy. Here is another one.

This particular check here, it says, pay to Galaxy for Sal Yeroham. And I had to give Galaxy money in addition! They gave me a $2000 check for bringing this man in as a $5000 franchisee and then the made decided he only wanted a $2000 field manager's position, which meant I had to

give them $1250 back but I was entitled to $2000.

But they talked me into giving them the $1250 back, which I had to do. Otherwise they told me I wouldn't get any more money or franchises. So this is part of it and I gave them more in addition to that. Here, this one, in all debts due and payable on Sal Yeroham and Mel McLean, we're even, Arthur Shevack, and I signed it on the back.

Here is another $1050 on the McClean deal that I got beat out of.

These, I assume I received. But I don't know why I received them.

Q Let me ask you a question, Mr. Shevack: On all these checks in front of you, do the backs of the checks reflect your signature?

A Yes.

Q On every check? Please make sure, Mr. Shevack.

A In other words, you are asking me if I can verify the fact that this in fact is my signature on the back of every check.

Q Yes. Does your signature appear on each and every check?

A My name appears.

Q Your signature?

A Yes. It looks like my signature. Some look like they're very hurried. It's possible they're not but I think they all are, yes.

THE COURT: Is there any doubt in your mind that any of those handwritten endorsements are not in your handwriting?

THE WITNESS: Well, there is one particular check that if I signed my name this badly, it's -- it's very unusual. I don't ever recall signing my name this way. Although above my name it says, "Pay to Galaxy Foods," which does look like my signature.

If I saw the stub, in other words, the reason I received this check, if I could see the bottom half of this, I would be able to say I did or didn't receive it.

The way it appears here, it's one of many, which are exact duplicates of one another.

THE COURT: Regardless of whether you received the proceeds of the check, my question is: Is there any doubt in your mind that the handwriting on the back is yours?

THE WITNESS: No, I'll go along. I'll say that all of these are my signatures.

(continued next page.)

Q Mr. Shevack, where are the check stubs?

A What?

Q Where are the check stubs on the check I showed you?

A The stubs are normally given to me but I use the same type of checks in the corporation I am in now and you have a carbon copy to the check.

Q You said you got the check stub, I am asking you where they are today.

A Burned, in the garbage. Thrown out a year ago. I don't save them.

Q You threw them out?

A Yes.

MR. GARMANSKY: I would like to mark as Plaintiff's Exhibit 42, these checks as one group.

MR. GOIDEL: Your Honor, I appreciate it if they could be -- well --

THE COURT: We can make them A, B, C.

MR. GOIDEL: Yes, because he did refer to certain ones specifically.

MR. GARMANSKY: He did identify them by date number.

THE COURT: If there is to be some question about some of them it is better to give them one number

than separate letters. How many are there? Did you say 14?

MR. GARMANSKY: Approximately that many, your Honor.

THE COURT: Fourteen he said originally. What is our next number?

THE CLERK: 42.

THE COURT: Make it 42A through whatever letter it is.

THE CLERK: Okay, your Honor.

MR. GARMANSKY: There are 14 of them here, your Honor. I would like to have them in chronological order.

THE CLERK: All right.

MR. GOIDEL: I have no objection to their introduction.

THE COURT: I was just about to ask you that.

THE CLERK: Fourteen checks 42 to 42M inclusive, marked in evidence.

(So marked in evidence.)

Q Mr. Shevack, do you recall receiving Plaintiff's Exhibit 42 as a commission sponsoring a new person into Galaxy? It's check number 1610.

A I assume I received it. I don't know for what.

I know for bringing somebody in but I don't know who.

Q Woudl it refresh your recollection, check #1610 is listed in the override commissions column of the books and records of Galaxy marked Defendant's Exhibit G.

A What did I do? I brought somebody into the firm who I assumed purchased a field manager's position from the corporation. Who the individual was, I don't know. I know what I did. I don't know who bought the business.

Q I am not asking you who, I am asking if it is an individual.

A Yes.

Q Plaintiff's Exhibit 42A is a $2,000 check, do you recall receiving that?

A (No response.)

THE COURT: What was the amount of 42?

MR. GARMANSKY: 750.

THE COURT: And 42A?

MR. GARMANSKY: $2,000.

A I received it but it is paid to the order of Galaxy Foods on the back. I signed it, endorsed it, and gave it back to the company.

Q Did you get the money, Mr. Shevack?

A I don't know.

Q Why would you give Galaxy $2,000?

A There is one instance on Sal --

Q This check --

MR. GOIDEL: Just a minute. Let him finish his answer.

A I recall a specific instance when I had to give back money that I received for a check. I don't know if this is the way the bookkeeping went or whatever the case may be. Sometimes, although receiving one of these checks, I owed it to the corporation and I had to give it back to them.

Q Was that the check marked Plaintiff's Exhibit 42A?

A This is marked 42A.

Q Is that the check that you gave to Galaxy and did not receive the money stated on that check, $2,000?

A Sir, honestly without knowing who I got the check on, I don't know. You showed me 14 checks or 10 checks or whatever it was. I don't know. I don't know why I got the check. To recall this in my mind -- I don't remember if it is 1746.

Q Mr. Shevack --

MR. GOIDEL: If the stubs are available, the witness stated by looking at the stubs if they are available, it could speed up the testimony. If they are available. I don't know if you have them. Can we show them to the witness simultaneously to the check?

That's all I suggest.

THE COURT: Are there stubs available?

MR. GARMANSKY: I don't know whether or not we have the stubs for Mr. Shevack's checks.

THE COURT: There have been occasions when you have received a check and asked for cash and that would have been the reason for giving the check back?

A It is very possible, yes.

MR. GOIDEL: Again, may we approach the bench, I don't want to say it aloud to appear I am putting words in the witness' mouth.

(The following took place at side bar.)

MR. GOIDEL: We are not trying to be evasive, the witness did refresh his recollection from income tax returns, there was a 1090 provided by the corporation showing that the net received by him for the year in question was $11,500. I don't want to say it aloud but I think that instead of beating a dead horse we can get right to it and find out what it is. He will not be able to explain on an individual check basis, not that he is trying to be evasive but --

MR. LERNER: Mr. Goidel was permitted to do it with prior witnesses. It's a question of testing his memory, credibility, and I think that we should be

allowed to do it. He hasn't produced a W2 form.

MR. GOIDEL: He didn't ask.

MR. LERNER: You put him on on direct. You brought out $11,000.

THE COURT: I will permit you to ask him about the various checks. You may go ahead. I realize that it is time consuming but we will have to endure it. I think it is better to go through it one by one.

MR. GARMANSKY: All right.

(The following took place in open court.)

Q I am showing you the next check marked Plaintiff's Exhibit 42B. Do you recall receiving that money?

A Yes.

Q Was that for sponsoring of a new individual into Galaxy?

A Yes. All these checks are.

Q I show you -- what do you mean all these checks are?

A I guess they are for the same thing.

Q Do you know that for a fact, Mr. Shevack?

A I am assuming it is so. I don't know until I see the stubs.

Q That's why I am asking to show you each one. Do you recognize Plaintiff's Exhibit 42C?

A Yes.

Q Did you receive that money, $750 on Plaintiff's Exhibit 42C for sponsoring a person into Galaxy?

A Yes.

THE COURT: What was the amount of 42B?

MR. GARMANSKY: 42B, $750. 42C is the same.

Q Check number 42D, Mr. Shevack, was $750, did you receive that?

A Yes.

Q For sponsoring a new individual into Galaxy?

A Yes.

Q Check number 42E for $1,250, did you receive check number 42E for sponsoring a new individual into Galaxy?

A No. This check -- somebody was a field manager from the looks of the amount, it looks like they became a distributor and it is the same person who invested more money.

Q This $1,250 listed on 42E, did you get this money, Mr. Shevack?

A You see, honestly I can't answer the question. I can't answer honestly.

Q Is that your endorsement on the back of the check?

A Yes. For what I earn it for, I don't know. Look, I could have been a distributor which I was, assuming

you were a field manager, okay? And you sponsored someone in the business and assuming you were Mr. Melvin McLean, you brought in three people for argument's sake and you were entitled to receive $1500, but all the checks would have been written out to Artie Shevack, not Melvin McLean -- are you asking if it is mine? I would say yes. But not mine because Mr. McLean got it. Until I see the carbon copy I don't know. I can't tell you.

Q Do you recall what this $1,250 was for?

A No.

Q Now, if Mr. McLean was part of your organization as a field manager --

A He wasn't.

Q Assume that he was.

A I would have received a check for I believe it was $750.

Q Please let me finish. Assume you already received your commission on Mr. McLean and he joined as a field manager and you are a distributor, Mr. McLean is part of your organization?

A Yes.

Q Suppose Mr. McLean brings in a field manager.

A Yes.

Q Isn't it a fact that you would get some part of

the commission when that person that Mr. McLean brought in joined Galaxy as a field manager?

A Yes.

Q You would get approximately $250, wouldn't you?

A Yes.

Q Would you get the entire commission from this individual who Mr. McLean brought in of $750 and give Mr. McLean $500 or would he get his own check?

A On two occasions that I can recall, although he should have gotten his own check, it did not. The check came to me and I then had to pay this individual the $500 he would be entitled to. Branch Simmons for one, on two occasions if you show me the stubs I can pick them out. I believe one was Al Jackson. Somewhere in this stack there is a check made out for $750 for Al Jackson. Branch Simmons would be entitled to $500. The check never came in his name, it came in mine. I had to write him a personal check which I have a copy of and I sent him at the end of the year a tax form that my accountant filled out. That is income classified as mine but I never got it.

Q You are saying on some occasions out of the checks you received from Galaxy you were obligated to pay other people that money?

A Yes.

Q But you are not sure exactly from what checks?

A All they are are duplicate checks from one another.

Q You are not sure from which checks?

A No.

Q The next check, Plaintiff's Exhibit 42F for $750, did you receive that for bringing in new people to Galaxy or is it an additional override in your organization?

A The amount stated -- I should have a receipt for bringing in a new person into Galaxy Foods. But on the back of said check paid to the order of Galaxy Food, which means it is possible I received it and it is possible I did not receive it. It's possible they cashed the check for me and they felt I owed them this money for some purpose.

Could I ask a question, your Honor?

THE COURT: Just a minute.

MR. GARMANSKY; I move to strike the portion of Mr. Shevack's testimony where I asked him did you receive that check and he went into the speculation.

THE COURT: Of course the speculation is generated by your repetition of the statement, did you receive it on behalf of this or that. The question is, if you simply want to ask him whether he received the check on a one by one basis, then his answer should

be yes or no.

MR. GOIDEL: Or I don't know.

THE COURT: Whatever.

MR. GARMANSKY: Thank you, your Honor.

(Continued next page.)

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Q Mr. Shevack, I show you Plaintiff's Exhibit 42-G for $1,250, did you receive that check?

A Yes.

Q Plaintiff's Exhibit 42-H, did you receive that check?

A Yes.

Q The same with Plaintiff's Exhibit 42-I, did you receive that check?

A No.

Q Does your signature appear on the back of 42-I?

THE COURT: He already testified his signature appears on the back of each one.

Q Did you receive Plaintiff's Exhibit 42-J?

A Yes.

Q Plaintiff's Exhibit 42-K?

A No.

Q Plaintiff's Exhibit 42-L?

A No.

Q Plaintiff's Exhibit 42-M?

THE COURT: Let me say this, I didn't mean you have to say yes or no; if you can't recall, you are privileged to say that.

A I don't recall.

THE COURT: It is endorsed by you on the back?

THE WITNESS: Yes. I agree that the endorsement is mine.

THE COURT: I understand. At this point you can't answer the question yes or no, meaning the proceeds of the check?

THE WITNESS: Yes, because -- you know, if you look at them, pick out which one was for this individual or this one for that individual, which one did an individual bring in that I paid him. I cannot give you that answer. I am willing to, I just don't know which check is which. There is a book somewhere here.

THE COURT: Would it prove at the very least you received some part of each check that has been shown to you?

THE WITNESS: I either received all or nothing of each particular check. Either I received the check or I had to give it back to Galaxy Foods or give that to somebody else. Let's say a Branch Simmons, who was a field manager. In error they may have made out the check to me when it should have been him. And rather than go through the time-consuming procedure, I wrote a personal check. I can verify this, that I wrote the check. The tax returns I filed state that.

Q I show you Plaintiff's Exhibit 42-L, the amount is $982.42. Do you recall why that amount was payable to you?

A No, I have no idea.

Q Did you ever receive such an odd amount for a commission?

A It is possible, in the event that the person who bought a franchise -- I would say to them, all right let the guy owe me the money. That is a possibility.

Q The person who bought a franchise?

A Let's assume I was supposed to get $2,000 for a man joining the corporation and he was short 1,000. He only had 4,000 to buy a business and didn't have the five necessary. I might receive a check for $1,000 instead of $2,000. If I went to the corporation and agreed that O.K., if you accept the $4,000, he owes me one thousand dollars personally and I will pay for part of his franchise.

In other words, I didn't receive the full commission at all times.

Q Are you saying, Mr. Shevack, that the person buying this franchise made an agreement with Galaxy not to pay the full amount?

MR. GOIDEL: Objection. That is not what he said.

A He pays the full amount and I am in essence lending him the money.

Q You are giving him part of your commission?

A Yes.

Q Did you ever do this?

A Yes.

Q To whom?

A Steven Silverman, he still owes me money.

Q How much?

A At least $200.

Q Anyone else?

A I am trying to think. If you can give me the names of those (indicating), I can tell you.

Q Do you recall anyone else?

A McLean. I don't remember, might have been some, but I don't remember.

Q Mr. Shevack, you first talked to Mr. Lieberman in June of 1971 about Galaxy, is that correct?

A June '72 -- The phone call?

Q Yes.

A Yes.

Q Then the next time you saw Mr. Lieberman and talked about Galaxy was June of 1972, is that correct?

A Yes, I believe so.

Q In June of '72, you decided to become associated with Mr. Lieberman's organization and work your way in Galaxy?

A Yes.

Q Did anything occur between those two dates, June '71 to June '72, to change your mind about becoming associated with Galaxy?

A Yes, I became disenchanted with Koscot.

Q You were in Koscot up until June '72?

A Yes.

Q Why did you become disenchanted with Koscot?

A I didn't like the way it was run. I couldn't get my merchandise and products to sell. The relations were changing. The method of operation was changing. You had to wait months and months out of stock. They didn't have the merchandise. I am serious about that.

During two days of Christmas I sold over $2,000 worth of products and they had a warehouse on Eighteenth Avenue in Brooklyn. I had more stuff in my store than they had in the warehouse.

Q Mr. Shevack, were you required to open up a store or boutique, like the one you did in Koscot? Was that part of your requirement to become associated with Koscot?

A No, it wasn't a requirement to do anything.

Q Thank you. All your expenses that you had in

connection with Galaxy which you so thoroughly went over in your direct testimony, did you take that off your tax return as a business deduction?

A The ones that were applicable I did. The ones I was allowed to I did.

Q The ones you talked about today, gas, guests at meetings, all those expenses, did you take those off?

A Yes.

Q Now, how many people, Mr. Shevack, did you personally sponsor into Galaxy?

A Seven, ten.

Q Do you know a Melvin McLean?

A Yes.

Q Did you sponsor him into Galaxy?

A Yes.

Q Did you have any discussions with Mr. McLean about his financial capability to join Galaxy?

A I think I did. I told him that he didn't have a dime. He couldn't rub two nickels together.

Q I didn't get your answer.

A Mr. McLean --

Q He said he --

A I told him he couldn't -- he wasn't able to join.

Q What did Mr. McLean tell you to lead you to that opinion?

A I don't recall his job status at the time, I remember he came down to an opportunity meeting one night and he was enthusiastic about joining. I said, "O.K., do you have the money to join?"

He said, "No, I don't have any money at all to join."

I discussed his job with him. The way it looked to me he didn't have a hope or a prayer of getting into the corporation. He told me he could get up a deposit. Once he did get up a deposit I allowed him to work in the rest of the way because I felt he was very serious. And as it is, he turned out to be successful.

Q How much money did Mr. McLean give you for the deposit?

A Approximately 25 percent, 30 percent. Something like that.

Q Of what?

A Of the $2,000 necessary.

Q He gave you 500?

A Five, seven, something like that. I don't recall.

Q About how much do you recall? What is your best recollection?

A Five hundred.

Q Five hundred?

A I would say 500.

Q How was this 500 given to you, check, cash, how was it given to you?

A I don't recall. It should say on the application whatever it was.

(Continued on next page.)

Q Why should it say on this application, Mr. Shevack?

A I would have given him a receipt of some type.

Q What do you mean by "application", Mr. Shevack? You mean, the contract that Mr. McLean signed to join?

A Yes. Originally it should have had the amount of deposits on it. If he didn't have the contract with him when he joined or when he gave me the deposit, I would have handwritten a receipt and gave him one.

Q Do you recall putting in on an application, the $500?

A I don't recall. I don't recall what transpired, but I know he gave me a deposit of some type.

Q Well, Mr. Schevack, were you instructed by anyone what to do when you get a deposit of money towards the purchase of a franchise?

A Yes.

Q What were you instructed to do?

A To hang on to it because the corporation doesn't accept deposits.

Q They don't accept deposits?

A They want pieces of it.

Q Who told you this?

A Mr. Roth.

Q Who else?

A That was it. I went to him with deposits on occasion.

Q Just Mr. Roth?

A Yes.

Q Okay. Did you go to Mr. Roth with your deposit from Mr. McLean?

A No, I don't believe I did.

Q Any reason why you didn't?

A He didn't want it.

Q How did you know that?

A Because he told me that previously.

Q Oh? How long ago did he tell you that he didn't want deposits until the time that you got Mr. McLean's deposit? How much time elapsed?

A Maybe two weeks, three weeks; something like that.

Q Whom did you go to -- whom did you see Mr. Roth about at the two weeks earlier than Mr. McLean? Did you have another person who gave you a deposit?

A Yes. I had somebody who wanted to join the corporation.

Q Who was that?

A I don't recall his name, but I know it was before Mr. Mc Lean because Mr. McLean is more vivid because I had a discussion about Mr. McLean.

Q So Mr. McLean gave you $500 approximately? That's your best recollection?

A Right.

Q And you kept it?

A Kept it.

Q Yes. You did'nt turn it in to Galaxy? You held on to it?

A At that time, okay.

Q What did you do with the $500?

A Nothing.

Q Where did you put it?

A Nowhere. I put it in my wallet and kept it until it was ready to be turned in to the corporation.

Q How long did you carry it around in your wallet?

A Until Mr. McLean earned enough to be registered with the corporation.

Q When was that?

A A month later.

Q That's your best recollection, about a month?

A About a month.

It could have been longer, but about a month.

Q You don't know what form this $500 was in? You are not sure?

A No. Honestly, I don't recall what it was.

Q Was it cash?

A It's possible it was.

Q You just put $500 cash in your wallet and carried that around for a month? Is that what you recall doing?

A Yes, very possible.

Q Okay. But you're not sure?

A No.

Q Could it have been a bank check, Mr. Shevack? From Household Finance Corp.?

A Anything is possible. It's possible.

Q Do you have a recollection of that?

A Doesn't particularly ring a bell.

Q Was it a fact that Mr. McLean did give you a bank check from Household Finance Corp. for $750?

A I don't recall if he gave me --

Q Or $700?

A Check or cash.

Q Whom did you finally give this check to?

A Which check?

Q Strike that.

Whom did you finally give the check or cash or any other form in which Mr. McLean may have given you $500? Whom did you finally give it to?

A Wait. Let me clarify it.

In the event I was given a check or cash, which would not have totalled at least $1400, $1200, around that area, I would not have turned it in because the corporation will not accept it.

They don't want it.

Q Did this policy ever change, by the way, that the corporation, Galaxy, would not accept part payments?

A It's possible, four -- four different people may have given different answers at different times, but, you know, there was no success with the corporation at all on my end, in trying to let them hold deposits.

Q Now Mr. Shevack, my question is, what did you eventually do with the $500, be it check or cash, which Mr. McLean gave to you?

A It must have been turned into the corporation.

Q Do you have a recollection of turning it in, Mr. Shevack, or do you have a recollection of just keeping it?

A Well, the mere fact that he's a franchisee is

very simply stated, the fact that it had to be turned in.

$2,000 had to be turned in.

Q No, it does not -- Mr. Shevack, please be responsive to my questions. Everyone must have. I want facts.

MR. GOIDEL: Your Honor, let me object at this moment.

Q Do you recall --

MR. GOIDEL: If Mr. Garmansky is trying to ask the witness, as I -- I am not even certain -- is trying to ask him whether, if he was paid the $500 in the form of a check, what he physically did with that check.

MR. GARMONSKY: No, that's not what I am asking.

MR. GOIDEL; That's not?

MR. GARMANSKY: No.

MR. GOIDEL: Then I misunderstand.

MR. GARMANSKY: Let me rephrase it.

BY MR. GARMANSKY:

Q Mr. Shevack, you've just stated, just testified that Mr. McLean gave you approximately $500. You don't know in cash, in a check. You don't know what from.

You said that you held it for approximately a month in your wallet.

What did you eventually do with this $500?

A I must have taken that $500 and maybe three other $500 that also accumulated during that time and gave it to the corporation when he purchased his franchise.

Q Where did the other three $500 comes from, Mr. Shevack?

A Well, I advised him that rather than, you know, go out on a limb, he was able to work in the same way that I did. He could find someone. If they wished to buy a business, he'd be entitled to receive a small part of that commission, and, therefore accumulate the necessary funds, because he wasn't able to get any money.

Q When did you get this other $1500 that you were holding for Mr. McLean?

A During the course of time from the time he gave me the deposit until the time he joined.

Q Okay. What did you do with the other $1500, besides the 5 he initially gave you? Where did you keep it?

A Probably the same place the first 500 was kept.

Q Putting it in your wallet?

A Either put it in my wallet, stapled to the

application. You're smiling, but it was turned into the corporation.

Q No, I am saying, your wallet is getting awfully thick, that's all.

MR. GOIDEL: Your Honor, you know, we are sort of belaboring a situation. Mr. McLean in his testimony, as I understood it, acknowledges the fact that he got his franchise. I don't know that's an issue in this litigation.

MR. GARMANSKY: This is important for this witness' credibility here.

BY MR. GARMANSKY:

Q Now Mr. Shevack, then you accumulated $2,000 in your wallet and you paid it to Galaxy on behalf of Mr. McLean; is that correct?

A Yes.

Q And then Mr. McLean was given his franchise; is that correct?

A Yes.

Q Now MR. Shevack, do any of the checks which you have just reviewed concern anything about Mr. McLean?

A I explained to you, sir, that I don't know until I see a photocopy or something of the original.

Q Okay. An original check? This is the

original check.

A No, the --

Q The check stub?

A The stub, the carbon.

Q Okay, here. Plaintiff's Exhibit 42K in evidence. On the back of the check it says -- well, do you recognize the handwriting on the back of 42K, Mr. Shevack?

A That's my handwriting.

Q Would you please read it to the Court?

A "In all debts due and payable on Sal Yeroham and Mel McLean."

Q Yes. This check is for $1050?

A Yes.

Q Upon reading that statement, what is your best recollection as to what this $1050 was used for?

A Sal Yeroham.

Q How about Mel McLean?

A Mel McLean. I saw his name on another check, I think. Didn't I?

Q Okay. Please find it, if you did.

Well, we'll search for that other check. Just concern yourself with 42K. It says Mel McLean?

A It has two names on the back of that check,

not one.

Q Yes, Mel McLean and the other gentleman, Sal Yeroham?

A Yeroham.

(Cont'd on next page.)

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CROSS-EXAMINATION

BY MR. GARMANSKY: (Cont.)

Q Now, what did Melvin McLean have to do with Plaintiff's Exhibit 42K, the check for $1,050? Would you please explain that?

A WHat did he have to do with it?

Q Yes.

Why is his name there? Melvin McLEan's name? Why did ycu put his name on the back of that check?

A Because Mr. McLean was short money to become a franchisee and I had put up some money in order to -- that he reach the full amount necessary to be registered.

Q Mr. Shevack, you've just stated that you accumulated $2000 in your wallet on behalf of Mr. McClean and when you got the money you paid it to Galaxy so he could get a franchise.

Now, you are saying he was short? I really don't understand your testimony. Please explain it.

A You can't understand my testimony?

Q No, I don't.

A It's very simple to understand. Mr. McLean -- we had a dicussion about in the office. Now, Mr. McLean was under the assumption that he was supposed to be earning more than I had discussed with him, that he would earn on

sponsoring someone into the corporation.

He therefore felt that he didn't receive enough percentage, enough commission, on the three individuals he sponsored in and felt he was entitled at that time, after sponsoring three people in, he felt he was entitled to accumulate $2000 to receive a franchise.

Now, I had discussed it with him and he knew that he wasn't entitled to received $2000 in full at that time because he still had more work to do before he could get $2000. Because he was assuming, he was going to earn $5000 by bringing someone into the corporation.

All he invested was something like five or seven hundred dollars. Now, if a man pays $2000, he would have been entitled to receive a $500 commission. So I don't know why he felt that he was entitled to receive the same thing a man putting up three times the amount of money would be entitled to.

THE COURT: In other words, your point is that to the extent that a man underpaid, then it was your position his commission should be prorated accordingly.

THE WITNESS: Right. Mr. McLEan --

THE COURT: No. Is that correct?

THE WITNESS: Yes.

THE COURT: Is that what you just told us?

A Right.

THE COURT: Let me ask you this: What's the date of that check?

MR. GARMANSKY: 42K, your Honor.

THE COURT: Date.

MR. GARMANSKY: Yes. October 21, 1972.

THE COURT: Now --

THE WITNESS: I can elaborate further on this particular incident.

THE COURT: Let me ask you this:

Bearing in mind that as Mr. Garmansky has pointed out, you say you received some kind of deposit, forget the amount for the moment, but it was less than $2000 which Mr. McLean would have needed for field manager franchise?

THE WITNESS: Yes.

THE COURT: Which the testimony indicates he ultimately received, right?

THE WITNESS: Yes.

THE COURT: And you say that when you got his initial deposit, you just hung on to it?

THE WITNESS: Yes.

THE COURT: Kept it somewhere?

THE WITNESS: Yes.

THE COURT: You have mentioned a wallet but I don't know --

THE WITNESS:I'm not saying I kept it in the wallet. I normally don't carr, a wallet.

THE COURT: Did you have a business bank account of your own?

THE WITNESS: I did not put it in any bank account, no.

THE COURT: You did not.

THE WITNESS: I kept it wherever it was given to me, whether it be cash or check. I believe I still had it.

THE COURT: All right.

Now, MR. McLean went out and did some recruiting; is that correct?

THE WITNESS: Yes, he did.

THE COURT: Now, when he got somebody who actually signed up, that is, made his investment, whatever it was, paid it into Galaxy, what would that trigger as far as Galaxy was concerned, a check to you or a check to McLean?

THE WITNESS: A check to me.

THE COURT: In the same way as you explained earlier where you were working for Lee or Lieberman?

THE WITNESS: Yes. Exactly.

THE COURT: You were riding on his franchise?

THE WITNESS: Right.

THE COURT: And when you finished the trip, he got the check?

THE WITNESS: That is right.

THE COURT: And you are saying the same situation -- this is your testimony -- prevailed with respect to McLean?

THE WITNESS: Yes.

THE COURT: And maybe others like him, if any?

THE WITNESS: Right. The check came in my name.

THE COURT: The check came in your name. But the -- on that statement of debts, this -- on all debts due and payable on Sal Yeroham and Mel McLean.

THE WITNESS: Right.

Because if I could elaborate for a moment?

THE COURT: What do you mean by "debts" then? What is meant by debts ? You wrote that, didn't you?

THE WITNESS: Yes.

THE COURT: What did you mean by it?

THE WITNESS: The debts means money owed. To even out.

THE COURT: Money owed to Galaxy?

THE WITNESS: Yes.

THE COURT: So are you really saying then either you had previously received commission checks--

THE WITNESS: Which I did.

THE COURT: Which you did.

THE WITNESS: On behalf of Mel McLean.

THE COURT: On behalf of Mel Mclean.

THE WITNESS: Which I now had to give to Galaxy Foods.

THE COURT: Which you now had to give back. Why didn't you give your own check instead of Galaxy giving you a check? I don't follow that complicated kind of bookkeeping.

THE WITNESS: Because this -- this I believe happened on a Sunday. We were sitting in the office and McLean came in and I believe he was speaking to BRuce Katz. And Bruce came over to me and said: You know, you have a man here. I understand he's working into the corporation. He's not a member yet. But he says he's a little upset. He felt he should already be a registered franchisee and he explained to me the system by which he was being paid and he seems to feel at this point, looking back on it in retrospect

that it was a little unfair.

He feels that he should have been earning more money. I sat down with Mr. Katz, who was then, you know, in charge. He was vice president or president of something. You know. And he was discussing with me, why don't you do the guy a favor. Give him the higher commission. Why make a big stink about it. The hell with it. He says, you're right, so the heck with you're right.

THE COURT: Yes. But what I am trying to say is: Why wouldn't that debt have been paid by your check to Galaxy rather than a check issued by Galaxy to your order for $1,050 which you endorsed back to Galaxy?

THE WITNESS: Galaxy Foods would only take cash or a certified check, or, naturally, their own check.

They would not take a personal check on my behalf. AT any time. That is not the policy.

THE COURT: Are you saying that you got up a thousand and fifty dollars in cash?

THE WITNESS: No. Mel McLean -- I had whatever deposits and earnings Mel McLean had accumulated, that he was rightfully entitled to, it was short money.

But I will be entitled to receive a commission when that money was given to Galaxy in full. I would be entitled to receive a commission. What they did was cut the commission check and give it to me before I gave them any funds at all.

Now, I took the commission check that they just gave me, that I signed, that I supposedly received this income, added it to the other money, gave it to Galaxy Foods. I had nothing. I walked away.

THE COURT: That sounds like a very complicated--

THE WITNESS: It was very complicated.

THE COURT: -- way to handle a very simple transaction. But if that's your testimony, I guess that's the way we --

THE WITNESS: That's exactly the way it happened. Mr. Katz was there.

THE COURT: All right.

Now, Mr. Garmansky, where do you want to go from there?

MR.GARMANSKY: Thank you. A little further with it, your Honor.

THE COURT: All right. Don't beat it to death now, please.

MR. GARMANSKY: NO.

Q When did MR. McLean official join Galaxy, do you know?

A Officially, no. Whenever his contract is dated, I guess.

Q This is Plaintiff's Exhibit 33 in evidence. The date is October 8, 1972.

Does your handwriting appear anywhere on this contract, Mr. Shevack?

A Yes, it does.

Q Where does it appear?

A My handwriting appears -- wait a minute. No. This is not my handwriting.

Q None of it is; is that correct?

A That's Bruce Katz' handwriting.

Q Okay.

Did Mr. McLean ever ask you any time for his contract, Mr. Shevack?

A Did he ask him for it?

Q Yes.

A I never gave him his contract.

Q It's what what I'm talking about, Mr. Shevack. Please listen to my question:

Did Mr. McLean at any time ask you for his contract? "Please give me my contract; where is my contract?"

A Yes, he did.

Q How many times did he ask you, Mr. Shevack?

A Twice, I believe.

Q Did he ask you prior to October 8, 1972?

A Prior to October 8? I don't recall.

Q You don't recall?

A I really don't recall. October 8 is a date last year. That's all it is to me.

Q Fine. Now, why was Mr. McLean asking you for his contract, do you know?

A He was mistaken, that's why.

Q I don't understand.

A He supposed to get it from Bruce Katz who actually filled it out.

Q Supposed to get it from Bruce Katz?

A Yes.

Q How do you know that?

A Because Bruce Katz actually filled out the paperwork while we were sitting there.

Q In front of you?

A Yes.

Q When he asked you two times for his contract, did you tell him, "See Bruce Katz"?

A I did. I told him, "See Bruce Katz or Charlie

Horowitz was also there."

Later on he walked into the meeting.

Q Now, how many people did Mr. McLean sponsor into Galaxy prior to his signing his contract? Do you know?

A Two or three.

Q Okay.

And how much money did he received for sponsoring each person in while he was working in your organization like you worked for Mc. McLean?

A It was a progressive amount.

Q How much did he receive, approximately, for those three people.

THE COURT: Did he say two or three?

Q Two or three, for those two or three people?

A He received in actuality, at this point, $500.

Q Okay.

So did he reach his $2000 including the 500 he had initially given you, for the purpose of his field manage- franchise?

A What I'm saying is now he did end up with a franchise.

Q That's not what my question is, Mr. Shevack. Please listen to my question.

MR. GOIDEL: Now, I'm going to object for this reason, your Honor. I think there is some confusion. Obviously, there is ome confusion but I think the confusion is brought about in the mind of the witness and certainly in my mind because of what he believes Mr. McLean believed he was entitled to and what the witness may have believed Mr. McLean was entitled to and I don't know that we have established that the same figure was in the mind of both people.

Now, if we can get that established, I think we will move along very speedily.

MR. GARMANSKY: Your Honor, I think the question was very simple and the witness is evading the answer.

MR. GOIDEL: I think -- I'll object to the form.

THE COURT: I'm not sure exactly what you say is being evaded here.

I understand the general drift of this but I must confess that we are spending what I think is an inordinate amount of time on one event which -- the relevancy of which, to the issues in this case, I fail to see.

I believe that we'd all derive much more benefit

from some other transactions than this one. We've heard McLean's testimony. We know how it ended up. REally, what difference does it make if there was a controversy and whether Mr. Shevack's position was more hardnosed than it should be.

BY MR. GARMANSKY:

Q Now, Mr. Shevack, did you ever suggest to Mr. McLean to go to a bank and obtain a bank loan to join Galaxy?

A No.

Q Didyou ever talk to him about any kind of method for raising money?

A Friends.

Q Was that the only method?

A Yes, generally speaking, yes, I would say yes.

Q That was it? You told him just to see friends, if you don't have the money?

A Yes. I don't know -- I don't think he had a job. He had to go see a friend.

Q That's -- please answer my questions, Mr. Shevack.

A Yes.

Q I didn't ask you if he had a job. Did you ever suggest to Mr. McLean any ways to raise money? You've testified

friends. My question is: Is that the only method you told him in which to raise money?

A Yes.

Q Now, did you ever say -- strike that. Did you ever tell anyone else who wished to join Galaxy how to raise money?

A In general terms, speaking to people?

Q The question calls for a yes or no. Did you ever tell anyone else how to raise money if they wanted to join Galaxy?

A Yes.

Q Who?

A Specifically, I don't recall names but in general, I remember I discussed raising money with people, yes.

Q Fine.

Now, on those occasions did you tell those people only to see friends, if they wished to raise money or did you tell them more?

A I told them there were thousands of ways to get money.

Q Well, like what did you tell them, Mr. Shevack?

A I told them look in the newspaper. Thereare ads every day on where to get money. I told them, you can

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pick up any one of these wealth and success magazines. I says there are people willing to lend you money on anything.

Q Let me ask you this:

Did you tell any of them that they could take out a bank loan to join Galaxy?

A No.

Q You are sure of that?

A Yes, I'm sure.

Q I'd like to read from your transcript, September 17, 1973, the following questions and the following answers: Please tell me if you recall them. Page 68, line 9:

"Question: Did you ever state to Mr. Steve Silverman the possibility of taking out a bank loan among other ways of raising money to join Galaxy?

"Answer: Yes, I believe so.

"Question: You have a recollection of that?

"Answer: Yes."

A I don't recall that's what I stated.

Q Let me ask you the question: Do you recall --

THE COURT: All right.

Don't beat it to death, please.

MR. GARMANSKY: I just wondered if he recalls the answer.

THE COURT: He said yes.

MR. GARMANSKY: Okay.

Q Now, did you take Mr. Melvin McLean to the bank of North America?

MR. GOIDEL: Excuse me, your Honor.

You just made a statement. May I hear the answer of the witness and the statement that came subsequent, just to --

THE COURT: Yes.

(Record read.)

MR. GOIDEL: No, your Honor, I don't believe he said yes.

THE COURT: Read back a little further now. Let's see back to where the transcript was read and what his response was to the read portion.

(Record read.)

(continued next page.)

lfws.

MR. GOIDEL: I don't know if your Honor follows what I was saying.

THE COURT: I follow it clearly. In my opinion, it is totally unimportant.

MR. GOIDEL: Okay.

MR. GARMANSKY: Your Honor, I would like to show the witness the transcript, since he does not recall.

THE COURT: You may show it to him.

THE WITNESS: I recall the context in which I stated that. It was a little different than the way you are asking questions at this time.

THE COURT: Mr. Shevack, there was no reference to any context. The basic questions is, Did you appear at a hearing before Commission officials on September 17, 1973, where you were placed under Oath and asked certain questions, and you gave certain answers?

THE WITNESS: Yes.

THE COURT: Is one of those questions and one of those answers that which was just read to you on page 68?

THE WITNESS: Yes, it was.

THE COURT: That's all there is to it.

As the Doctor says, it is painless.

Q Now, Mr. Shevack, do you know whether or not any person you sponsored into Galaxy did in fact obtain bank loans

in order to join?

A Most of the people gave me bank checks. I don't remember who or where. I got all different types of checks.

Q But do you know for a fact that some people did obtain bank loans in order to join Galaxy?

A No.

Q You don't know that for a fact?

A No. I received a check from a bank, it could have been a savings account, it could have been a loan, or anything. It was a bank check.

Q I am going to read the following questions and answers on page 70:

"Question: How do you know that he obtained loans, Mr. Silverman, this is, loans from the First National City Bank, and the bank on Avenue U or V in Brooklyn?

"Answer: He told me how he got the money.

"Question: He did?

"Answer: Yes.

"Question: He stated that he got a loan from the First National City, and another bank on Avenue U or V in Brooklyn?

"Answer: I lent Steven Silverman some money, too."

A Yes, but that is not what I know for a fact, that's only what Steve told me. Whether I know it for a fact, I don't know. That is third party.

Q Now, Mr. Shevack, do you recognize Plaintiff's Exhibit number 34?

A Yes, I do.

Q Did you have Plaintiff's Exhibit 34 printed up?

A Yes.

Q How many did you print up?

A 500. I don't know.

Q Did you hand these out, Mr. Shevack, Plaintiff's Exhibit 34?

A Yes.

Q Who did you hand these out to?

A People.

Q Did you know these people?

A No.

Q These were total strangers?

A Yes.

Q Did you ever stop anyone on the street and say, "How would you like to earn $50,000 a year?"

A It's possible.

Q Do you recall doing that to Mr. McLean?

A No.

Q How did you first meet Mr. McLean?

A How did I meet Mr. McLean?

Q Yes.

A He came down to an Opportunity Meeting. I had never met him before. He walked in and asked for me.

Q Did you ask him how he knew your name?

A He had this card. It might have been this card.

Q He walked in and asked for you, you never met him before?

A No.

Q Did you ever stop him on the street and ask, "How would you like to earn $50,000 a year?

A No.

Q This card reads: "Are you ready to earn $50,000 per year?"

Do you know anybody who earns $50,000 a year in Galaxy?

MR. GOIDEL: The statement doesn't say he knows anyone --

MR. GARMANSKY: My question is --

MR. GOIDEL: It says, "Would you like to --

MR. GARMANSKY: The card reads, Plaintiff's Exhibit 34, "Are you ready to earn $50,000 per year?"

MR. GOIDEL: Fine.

Q My question is, "Do you know anybody who earns $50,000 in Galaxy?"

A That said they earned $50,000?

Q That you know of?

A Yes.

Q Who?

A George Padilla.

Q Anyone else?

A The Executives were all saying they did, George told me he did.

Q It says, for $2,000, or $5,000, if not totally satisfied, guaranteed money-back investment.

Now, was -- Strike that.

What does that mean to you, Mr. Shevack?

A What does it mean to me?

Q Yes.

A It means 2 or $5,000 guarantee investment.

Q You put this on the card, did you not?

A Yes.

Q If not totally satisfied, guaranteed money-back investment. You put it on the card?

A Sure.

Q Tell me what you had in mind, the reasons underlying putting that on Plaintiff's Exhibit 34?

A Because people would read it and come down to the Opportunity Meeting.

Q That was your sole purpose in putting it on?

A To have them join a corporation. They couldn't join unless they came down.

Q Did you use that as an inducement?

A Yes, it was approved by the corporation.

Q What was?

A This card (indicating).

Q Who did you show it to.

A Steven Katz -- Bruce Katz, Steve Roth, Artie Lee and Charlie Horowitz.

Q You showed this card to them?

A Yes.

Q They all approved it?

A Yes, they loved it.

Q What did they say?

A Go get 'em.

Q And you went out, and you got them, is that correct?

A I gave the card out. If they came down, fine.

Q Now, Mr. Shevack, was there anything that you heard in Galaxy concerning the guaranteed investment?

A Yes, they told us our investment was guaranteed.

Q Did they tell you any specific rule or regulation under which it was guaranteed?

A Later they came out with a manuscript, I believe

it is the book they finally published.

Q That is Plaintiff's Exhibit 3, is that correct?

A (No response.)

Q Would you look at rule 21, page 9, on Plaintiff's Exhibit 3?

A (No response.)

Q Is that the rule for the guaranteed investment?

A No.

Q It is not?

A You said 21?

Q Yes, rule 21. Yes.

A Oh, A, B -- Wait a minute.

Q Did you ever read or hear about that rule before today?

A Yes.

Q What was the underlying statement for this guaranteed money-back investment, Plaintiff's Exhibit 3, Rule 21, was that the underlying reason for it?

A No. They had a buy-back option somewhere in here.

Q Other than Rule 21?

A Yes. Rule 25.

Q What is Rule 25?

A Six months subsequent to the commencement of full-scale retail operation, Distributors and Field Managers, regard-

less of their date of entry in Galaxy program, will be permitted to exercise Galaxy's Food final buy-back option. Distributors and Field Managers will be notified of their option to sell their Distributorships back to Galaxy Food, Incorporated at the original purchase, less any commissions earned.

That is a guaranteed investment. That's what the corporation told us, you can't lose. Distributors will be given thirty days -- Shall I read the rest?

MR. GARMANSKY: No, I believe we have enough.

THE COURT: This is after six months?

MR. GARMANSKY: After six months with full retail operations. Six months of full retail operations.

Q That was your understanding underlying Plaintiff's Exhibit 34, is that correct?

A Yes.

Q Now, was there any other rules and regulations if Galaxy never went into full retail operations?

A If they never went into full retail operations?

Q Yes. Could a person get his money back? Let's say Galaxy would not go into full retail operations,,could a person still get their money back?

A I don't recall. Can I look through here? I don't remember.

Yes, there was.

Q What was it?

A It was, they would get approximately 50 percent of their investment back if Galaxy Foods -- if Galaxy Foods couldn't get from 8 to 12,000 customers. They would get approximately 50 percent of their investment back.

THE COURT: This is another Rule?

MR. GARMANSKY: Yes, 21, your Honor. It's in Plaintiff's Exhibit 3. That is, if there is no retail food operation by June 30th, 1973.

Q Mr. Shevack, was there anything that you knew of in Galaxy that if a person was not totally satisfied with his franchise for any reason whatsoever, he could get his money back?

A Yes, the corporation would make restitution for some individuals on occasion who didn't want to be in the corporation any longer.

Q Who told you that, if anyone?

A Who told me that?

Q How did you come to know this?

A It was explained to me on the Sal Yeroham instance. That was one of them that I was forced to return. I forgot how much. $1100 in commissions I received.

Q Because he was not totally satisfied with his investment?

A He purchased a Distributorship, and on doing that,

I would be entitled to $2,000. He changed his mind later and told them, "I don't want to be a Distributor, I want to be a Field Manager." His investment was only $2,000 for that. They refunded $3,000 to him, and also told me, because the refund was made to him, he wasn't satisfied with that position, you've got to give us back, because we gave to him, the amount of money that you were overpaid on that commission.

Q But it was your understanding if a person was not totally satisfied he could have his money back, anyone?

A I don't know about anyone.

Q What does your ad say?

A 2 or $5,000, if not totally satisfied, guaranteed money-back investment.

Q Thank you.

Mr. Shevack, do you know a Branch Simmons?

A Branch, yes.

Q Did you sponsor him into Galaxy?

A Yes.

Q Did you ever take Mr. Simmons to a bank in order to get a loan to join Galaxy?

A No.

Q Did you ever tell Mr. Simmons to put down on any loan application that the loan was for furniture, and not to join Galaxy?

A No.

Q Now, Mr. Shevack, if I were to tell me that Mr. Simmons testified that you took him to the bank and told him to put furniture on the loan application, would he be in error?

A Yes, he would be.

Q Do you recognize this document, Mr. Shevack?

A It's a loan application for furniture for Branch Simmons.

Q Do you recognize it?

A No.

Q Isn't it a fact your handwriting is on that application, other than Mr. Simmons' signature?

A No.

Q It is not?

A No.

MR. GOIDEL: May I see it?

MR. LERNER: It is not in evidence.

MR. GOIDEL: It doesn't have to be in evidence. If it was shown to the witness, it doesn't have to be.

THE COURT: No, it has been shown to the witness on the stand.

MR. GOIDEL: I think it should be marked for identification at this point.

MR. GARMANSKY: I would like to mark as Plaintiff's

Exhibit 43, a Xerox copy of an installment loan application.

THE COURT: What is the number?

THE CLERK: 43, your Honor.

In order not to deface the document, I am placing a piece of paper, and putting my sticker on the paper. 43 for identification.

MR. GARMANSKY: This document, the Court is aware, we did not have th document at the time Mr. Simmons was on the stand. The document was acquired this afternoon from the Bank of North America.

MR. GOIDEL: May I ask --

THE COURT: Let me ask you this, I missed what the witness said. Had he seen the document?

MR. GARMANSKY: The witness never seen the document before.

MR. GOIDEL: He said it is not his handwriting, also.

MR. GARMANSKY: Our invesiigator did go out to Hempstead and pick it up. In lieu of having a bank officer to put into put it into evidence, if Mr. Goidel objects --

MR. GOIDEL: I have no objection to the fact that the bank maintained this loan application in the regular

course of its business. I have no objection to the fact that this is a photostat. I am not going to insist upon the best evidence rule. It is not to be deemed an acknowledgement that the witness has acknowledged it was prepared by him.

MR. LERNER: I think that is clear on the record.

THE COURT: You are willing to waive the best evidence rule?

MR. GOIDEL: As to authentication.

MR. LERNER: Thank you.

THE COURT: It is a loan application, is that what it is?

MR. GARMANSKY: Yes, a loan application.

THE COURT: Of what bank?

MR. GARMANSKY: Bank of North America.

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(continued on next page.)

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CROSS-EXAMINATION

BY MR. GARMANSKY: (Cont.)

Q Mr. Shevack, do you recognize Plaintiff's exhibit 32?

MR. GOIDEL: 32?

Q 32.

THE COURT: That's already in evidence.

MR. GOIDFL: May I see it for my edification?

MR. GARMANSKY: Yes. It's an invitation card.

MR. GOIDEL: Oh.

A Yes.

Q Did you have Plaintiff's exhibit 32 printed up?

A Yes, I did.

Q How many did you have printed up?

A 500.

Q Did you hand those out to strangers on the street?

A Yes, occasionally.

Q Do you recall handing one to Mr. McLean?

A I believe that is the card he received.

Q Do you recall handing it to Mr. Melvin McLean?

A No, I don't recall handing it to him.

Q Mr. Shevack, how did you first meet Branch Simmons?

A Mr. Simmons? I was lost in Long Island and I asked him for directions.

Q Where were you going at the time?

A I was going for an opportunity meeting of Galaxy Foods.

Q Did you take Mr. Simmons along?

A Yes.

Q Did he go into the opportunity meeting with you?

A Yes.

Q Did you try to induce Mr. Simmons into joining Galaxy?

A Yes.

Q Now, you know Mr. and Mrs. Silverman, is that true?

A Yes.

Q Now, you were Mr. Silverman's sponsor into Galaxy, isn't that true?

A Yes.

Q Did you ever pick Mr. and Mrs. Silverman up and take them to a Galaxy meeting?

A Yes.

Q When for the first time?

A I think we went to the Holiday Inn one night in Manhattan or the Summit Hotel, I forgot where. I can't recall

enough to give you specifics. I assume it is approximately October. Possibly November of 1972.

Q What kind of a car did you have then?

A I had my car, a '72 Cadillac.

Q El Dorado?

A Yes.

Q Did you ever have any discussion with Mr. and Mrs. Silverman about borrowing money from a bank in order to join Galaxy?

A No, I don't believe so. Not directly. Not to go to a bank and borrow money for Galaxy Foods.

Q What do you recall?

A In relationship to how to get money, it might be possible that I discussed, you know, some thsources of how to get money such as I was going over before. There are newspaper ads or advertisements or friends or relatives or neighbors, that's what I meant by that question before.

Q Now, did you ever take Mr. and Mrs. Silverman around to different banks and finance companies in order to obtain loans?

A No.

Q You are certain of that?

A Yes, I am certain.

Q I would like to show you Plaintiff's exhibit 37.

Did you ever give Plaintiff's exhibit 37 to Mr. and Mrs. Silverman?

A No, I did not.

Q Plaintiff's exhibit 37, none of it is in your handwriting, is that correct?

A Right.

Q Do you know who Francis Alexander is?

A No.

Q Never heard the name before?

A No.

Q How about A & M Dental Labs?

A No. Francis Alexander?

THE COURT: Is that C-I-S or C-E-S?

MR. GARMANSKY: C-I-S.

A No, I don't think so.

Q You are not sure?

A I don't think I know him, no.

Q You are positive you do not know him, did you say?

A Yes.

Q Are you sure it is a him?

A Him, her.

Q I would like to show you Plaintiff's exhibit 36. Did you give this to Mr. and Mrs. Silverman?

A No.

Q Do you know what it is, Plaintiff's exhibit 36?

A It is a tax statement that you get at the end of the year.

Q A wage statement of how much money a person earns in employment?

A Yes.

Q You never gave that to Mr. and Mrs. Silverman?

A No.

Q Plaintiff's exhibit 41, Mr. Shevack, is this entire document in your own handwriting including the numbers?

A The vast majority of it is in my handwriting but there are things on it definitely not in my handwriting.

Q Such as what?

A This, 133175 with a line. This 6366.77 with a dollar sign and circle around it.

Q Anything else not yours?

THE COURT: Perhaps it wouldn't be a bad idea to take a red pencil and circle the items that he says are not in his handwriting.

Q Let the record reflect I am circling $6,666.77.

A Right.

Q Also the figure $1,331.75.

Anything else, Mr. Shevack?

MR. GOIDEL: Your Honor, I don't mean to interrupt testimony. I do have to make a call and I have to make something else. I am told Mr. Garmansky will probably finish up this evening.

THE COURT: I am hoping so.

MR. GOIDEL: If it is not a burden to the Court, I would like to take not more than 5 minutes.

MR. GARMANSKY: May I just finish this?

THE COURT: Yes.

BY MR. GARMANSKY:

Q Is there anything else?

A I believe just these two.

THE COURT: Anything on the reverse side?

MR. GARMANSKY: No.

THE WITNESS: The writing on the paper itself, the printing is naturally not mine. The name and Galaxy.

MR. GARMANSKY: The letterhead, that we understand.

THE COURT: This is a piece of paper with the printing on it, this is something that you've seen before?

THE WITNESS: Yes, it is Galaxy Foods' stationery.

THE COURT: There is no question about that?

THE WITNESS: No.

THE COURT: All right. Take 5 minutes.

(A recess was taken at this time.)

(Continued on next page.)

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CROSS-EXAMINATION

BY MR. GARMANSKY: (Cont.)

Q Mr. Shevack, I'd like to show you the affidavit which you signed and submitted to the Court.

It was signed on the 14th day of January, 1974.

MR. GOIDEL: Your Honor, in your absence we've already agreed to stipulate that that is an affidavit of Mr. Shevack and was submitted in this proceeding.

Q I'd like to point your attention to paragraph 12 in which you talk about a conflict between yourself and some of the other defendants, including the corporate defendant Galaxy.

Would you please tell us what you mean by paragraph 12, your explanation of it?

A This is where it states -- where it states, "Conduct on the part of the other co-defendants,"the majority of the other defendants were directors or owners of somewhat of the corporation.

I never was. I didn't speak at meetings. I didn't yell phrases like -- like I've heard, you know, "smell money in the room" or invite people up in front of the room to join the corporation. Or cheer. You know, This has nothing to do with me. I was one of over a thousand -- I

don't know how many people, 800 people that purchased from them and I sure wasn't the top of the list of people who weren't -- who earned lots of money. That's for sure.

I feel if I'm on trial here, let's get 800 other people here, too.

Q That's what you meant by the conflict in paragraph 12?

A Yes.

Q Now, Mr. Shevack, you testified that you currently are associated with Futuristic Foods; is that correct?

A Yes.

Q What position do you hold there?

A I am vice president.

Q Vice president?

A Yes.

Q Was that the only position that you've ever held in your association with Futuristic Foods?

A Secretary.

Q Any other positions?

A Well, president, but Mr. Cancilla is actually president of the corporation. He has been designated title-wise as the chairman of the board, which has moved me up to president.

Q Now, did you form -- form Futuristic?

MR. GOIDEL: Did he? I'm sorry.

Q Did you form Futuristic? Did you incorporate it?

A Yes, I was one of the individuals who incorporated it.

Q Who were the others?

A Peter Cancilla and Bill Reichert.

Q When was Futuristic incorporated?

A Approximately the early part of January, 1973.

Q Are you a shareholder of Futuristic?

A Yes, I am.

Q Were you a shareholder when it was incorporated?

A When it was incorporated?

Q Yes.

A Prior to incorporation or --

Q No.

When it was incorporated, were you a shareholder? Were you issued stock?

A Yes. Yes.

Q Now, approximately how long -- strike that.

Did you incorporate Futuristic approximately one month after you left Galaxy?

A Yes.

Q Who had the idea for Futuristic?

A I guess I did.

Q Did you have any experience in the food business prior to incorporating Futuristic?

A Nothing major, no.

Q How about Mr. Cancilla?

A No.

Q How about Mr. Reichert?

A Not to my knowledge, no.

Q What was the business purpose of Futuristic when it was incorporated?

A It was incorporated to take the best idea we've ever seen in our life and make it work properly, the way we knew we could and does now.

Q I don't believe you've answered the question.

What was the business purpose of Futuristic?

A To establish through a network franchises a corporation capable of servicing the needs of the consumer on a free home delivery service of name brand supermarket items, delivered to a consumer's home, without --

Q I'm sorry?

A -- without the obligations of freezers, contracts, of large volume orders that are necessary.

Q Did you get the idea for Futuristic from

Galaxy?

A I saw the concept at Galaxy, yes.

Q I'm sorry? I didn't hear you.

A I saw the concept at Galaxy Foods, yes.

Q Now, where was the capital to come from in order to start your food delivery service in Futuristic?

A The capital to come from?

Q Yes.

A It was the money necessary to run the operation, to set the operation up?

Q Yes. Where was it to come from?

A Well, the three individuals, we had investments in the corporation and also the franchisees that would join.

We would use the money they invested, a certain portion, for the equipment and the machinery necessary to carry out our service.

Q Now, what were the franchisees called, that you were selling in Futuristic?

A For illustration purposes or what were they actually called?

Q Did you have a name?

A No, just it was either a $2000 franchise or a $5000 franchise.

Q You didn't call them gold or silver?

A No, we didn't call them gold or silver, other than for illustration purposes.

We tried to designate a name because the investments have increased, where they would overlap. You couldn't just designate them a two or a three thousand dollar franchise. Because as they went up in value, the higher investment price at the lower level turned out to be the lower franchise price at the new investment level so it became confusing.

Q How much do the franchises cost today, Mr. Shevack?

A Three and six thousand dollars.

Q Now, how can an individual or how could an individual make money in Futuristic prior to August 23, 1974?

MR. GOIDEL: I'm sorry. Prior to?

MR. GARMANSKY: August 23, 1974.

THE WITNESS: Prior to August 23, 1974, he could acquire customers who he would deliver food to and he would receive his commissions on the sale of that food. Or he could sell franchises and earn a commission, in addition to that.

Q Now, after August 23, 1974, a person can only make money by obtaining customers to order food; is that correct?

A No.

MR. GOIDEL: Objection, that's not what he testified.

A After September.

MR. GARMANSKY: I'm not asking what he testified to. I'm asking if this is a fact.

THE COURT: I am confused.

MR. GARMANSKY: I'll rephrase the question, your Honor.

THE COURT: You mentioned an earlier date, prior to --

MR. GARMANSKY: To August 23, 1974.

Q My question is, Mr. Shevack, after August 23, 1974, the only way a person could earn money -- did this -- strike that.

Did this situation of making money ever change after that date?

A After which date?

Q August 23, 1974?

A Yes.

Q Now, isn't it a fact that the only way a person can earn money in Futuristic is by obtaining customers to order food?

MR. GOIDEL: Objection. You may -- Mr.Garmansky

I don't mean to be obstreperous. You may ask him how because your statement is not so. There are other wasy.

MR. GARMANSKY: Okay.

BY MR. GARMANSKY:

Q Mr. Shevack, how can a person make money in Futuristic today?

A Today?

Q Today?

A He will purchase a franchise, whatever franchise it happens to be. He will establish an amount of customers that are anywhere within the city limits, Westchester, Nassau, a portion of Suffolk. These customers will purchase merchandise. We deliver merchandise to them. Depending how much they are spending, he receives his respective percentage of what he's entitled to on a particular order.

Q Fine. HE can receive commissions from food?

A Yes.

Q Any other ways?

A That a person who buys a franchise?

Q No. Can he earn money in Futuristic? After he buys the franchise, any other way he can earn money in Futuristic?

A He could become an employee of the corporation. Not everybody, but if he files an application, if he's qualified, you know, he could do anything, be a truck driver. That's other ways.

THE COURT: You mean, being employed for salary or wages?

THE WITNESS: Yes.

THE COURT: Is that what you mean?

THE WITNESS: Depending on his qualifications, yes.

THE COURT: I understand.

If he's employed, he's paid a salary or wages?

THE WITNESS: Yes.

THE COURT: Even though he may also have a franchise?

THE WITNESS: Yes.

BY MR. GARMANSKY:

Q Mr. Shevack, must an individual buy the franchise to become an employee of Futuristic?

A No.

Q How many -- how many employees does Futuristic have?

A Approximately 60. Maybe more.

THE COURT: How many?

That's the total number; is that it?

THE WITNESS: Let me try to be accurate here. I would say about 60.

BY MR. GARMANSKY:

Q Are there any salesmen in those 60 employees?

A Salesmen? Yes.

Q What do these salesmen sell?

A Some of them sell franchises.

Q They're employed by Futuristic Foods?

A As an employee on a salary.

Q I see.

Is the salary determined by any criteria?

A Their background.

Q Are they paid the same salary every week?

A Yes. Most of the time. I mean, people are entitled to raises on occasion.

Q Are any of these salesmen franchisees in Futuristic?

A Yes, some of them.

Q Not all?

A Not all of them, no.

Q Now, can a person earn any money by sponsoring in new franchisees into Futuristic?

A Who?

Q Anyone?

A Anyone?

The only person who can sell a franchise is either the corporation or a corporation employee as a representative selling franchises.

He will not earn money on the sale of that franchise. He's paid a salary.

Q Is he paid a salary for selling a franchise?

A That's his job. But he gets paid whether he sells or not.

Q Please answer my question.

MR. GOIDEL: Your Honor, you know, if you mean, Mr. Garmansky, does he get an override commission, why don't you come out and ask him?

We're not playing cat and mouse.

MS. MYSLIWIEC: That's not proper objection.

MR. GARMANSKY: Your Honor, the witness did not answer my question. It's a simple question.

THE COURT: Let' have the question back and see if it's understood.

See if you can find the question.

(Record read.)

THE COURT: Well, did you understand the

question?

THE WITNESS: No. I am still not clear on this matter here.

Does a salesman get paid a commission for --

THE COURT: No. A salary.

THE WITNESS: Does a salesman get paid a salary for selling a franchise?

BY MR. GARMANSKY:

Q Yes.

A I'd have to say yes.

Q Now, is the salary dependent upon whether or not franchises are sold?

A No.

(continued next page.)

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CROSS-EXAMINATION

BY MR. GARMANSKY (Cont'd.)

Q It's not? The salesman will get a set salary per week, even if he does not sell franchises?

A Yes.

Q Have you had any salesmenwho have not sold any franchises?

A Yes.

Q Are they still employed?

A Yes.

Q Do they perform any other services as salesmen?

A No. They're salesmen. Some are sales managers, salesmen but they're all salesmen.

THE COURT: What I mean to say is, is there selling activity exclusively devoted to sale of franchises? Or do they sell the merchandise as well?

THE WITNESS: No. Their duty is to sell franchises.

THE COURT: And nothing else?

THE WITNESS: That's what they have been hired for, yes.

THE COURT: Right. In other words, do you

have salesmen who also seek out customers for food?

THE WITNESS: Yes. Wait. Excuse me, rephrase that. Our franchises seek out customers and they can hire salesmen to work for.

THE COURT: They are the ones who would hire salesmen for --

THE WITNESS: The food sales. We have management people, directing their efforts, trying to help them in their endeavors to sell food.

THE COURT: Right. But the only salesmen the corporation has --

THE WITNESS: Are franchise salesmen.

THE COURT: Are franchise salesmen?

THE WITNESS: That's right.

THE COURT: Some of those franchise salesmen do not themselves hold franchises, is that correct?

THE WITNESS: That's true.

BY MR. GARMANSKY:

Q Mr. Shevack, do --

THE COURT: Go ahead.

Q Do any of these salesmen, when they are trying to sell the franchises, tell the prospective franchisee or prospective investors Futuristic that they can also become salesmen too?

A They should not. That's not right and they are not allowed to.

Q Now, Mr. Shevack, are you certain that your salesmen get paid every week, whether or not they sell franchises?

A Yes. Yes.

THE COURT: Or at least regularly? Do they get paid every week?

THE WITNESS: Well, --

Q Every single week, there is no gap? There is no lapse?

MR. GOIDEL: Your Honor, I understand what you are saying.

Mr. Garmansky, would you please rephrase because I am not even sure. Do you mean every week or bi-weekly? It may be a bi-week rather than a weekly.

THE COURT: That is what I meant.

Q Mr. Shevack, when did you first employ these salesmen to sell franchises?

A We have been hiring salesmen ever since about the end of August.

Q 1972?

A Yes, up to and -- '74.

Q How many do you have now just selling franchises?

A Thirty.

Q Approximately 30 people?

A Approximately. Rough estimate.

Q Okay.

A We have got trainees. We have got salesmen.

Q Mr. Shevack, have these people, these 30 people, received a salary, either weekly or bi-weekly, but a regular salary?

A Yes. Every one of the men we have hired as a salesman received a paycheck and no one has yet been fired. If that is what you are asking. Everybody who was hired as a salesman is a salesman, is receiving a weekly paycheck and will continue to do so unless we feel the man is just unproductive and we'll terminate him. A salesman is paid to produce. We'll give him a trial period.

Q So, everyone of these salesmen have received a weelky paycheck?

A Yes.

Q No exceptions?

A No exceptions. Unless they didn't pick it up themselves. We're writing the checks. They're ready for --

Q Have any of these salesmen received any raises in salary, Mr. Shevack?

A Any raises?

Q Yes.

A Well, some --

Q Increase in pay?

A Some of them might have started with us on a part time basis and then decided, you know, they want to work full time. It is possible in that case we would have given them a raise. It is possible that one of the men was -- has better background than others or spoke to us that he couldn't survive on the income he was making. It is possible we gave him a raise, if we felt he was worth. If we felt he'd stick it out and be productive.

Q So some of them have?

A It is possible, yes.

Q Any of these raises ever been tied to the number of franchises that's been sold by the salesmen?

A No.

Q You're sure of that?

A Yes.

Q Have you -- did Futuristic sign any employment contracts with these salesmen?

A Employment contracts?

Q Yes. Being employed for stated period of time at a stated salary, anything like that?

A No.

Q In other words, these salesmen understand that they could be fired at any time? Let go?

A Yes.

Q Mr. Shevack, do you recollect this document? Xerox copy?

A Yes.

Q Would you please the Court what it is?

A This is the contract, of Futuristic Foods.

Q The contract of Futuristic Foods?

A Right. The contract brochure. It is prepared in brochure form.

Q This is what is given to prospective investors in Futuristic?

A No. This is -- it is not supposed to be given to prospective investors, unless you know they're ready to make a decision on the business actually.

Q I see. Does this explain the operation of Futuristic?

A Explain the operation?

Q Business operation.

A Yes, basically it does.

MR. GARMANSKY: I'd like to offer in evidence this document.

MR. GOIDEL: Your Honor, I'm going to object. I frankly don't see the materiality between this document and the issues before the Court in this matter involving these defendants in Galaxy.

THE COURT: It conceivably could have relevance to the question of relief. I was going to ask what the date of that particular document is.

MR. GOIDEL: I was going to also. There are two of them. One before August 23rd and another one subsequent.

THE WITNESS: Three. That one is outdated. It is obsolete at the present time.

MS. MYSLIWIEC: It doesn't make any difference.

MR. GOIDEL: Doesn't make any difference? I think --

THE COURT: As I say, I think it is relevant to relief and I am taking it on that issue, but I think also that if there are more up-to-date editions of it, possibly those should be made available to the Court too.

MR. GOIDEL: Frankly, your Honor, I don't have one here. I'll be very happy to get a copy of the

new --

MR. LERNER: We do not have any of the more recent editions.

MR. GOIDEL: Do you happen to have one you?

THE WITNESS: I wan't told I needed it.

THE COURT: Maybe counsel could stipulate that they could be made part of the record.

MR. LERNER: Certainly.

MR. GOIDEL: Sure.

THE COURT: Because it does seem to me that, by virtue of the limited nature for which this is being received, there ought to be an up-to-date --

MR. GOIDEL: For the edification of the Court, just simply --

THE COURT: Showing with respect to that issue.

MR. GOIDEL: The new contract will be very similar to this, with the --

THE COURT: I suspect --

MR. GOIDEL: With the exception of the complete elimination of the right to earn commissions on a basis of selling any franchises and eliminates the right of anyone to sell a franchise except -- well, eliminates the right of any franchisee to sell a franchise.

THE COURT: I might -- I wish to make it clear that i am not retreating on anything I may have indicated to you, but I understand there is a case pending in the Southern District of New York regarding Futuristic.

MR. GOIDEL: Yes, sir.

THE COURT: And it is not my intention to usurp the functions of the Court in that case. I am accepting this exhibit and any updated editions of it simply to take it into consideration with respect to the granting of relief in this case.

MR. GOIDEL: Your Honor, I will produce upon stipulation with counsel, I will produce the most up-to-date, which is the only other copy. It is not as though there were three or four other types. The only other type which went into effect subsequent to August 23, 1974.

THE COURT: That one has been marked what, now?

THE CLERK: Marked Plaintiff's Exhibit No. 44 in evidence.

(So marked)

THE COURT: All right.

THE CLERK: 13 page document.

THE COURT: Is there a date on it?

THE CLERK: All it says, your Honor, Futuristic Foods, Inc., 1973. It is undated.

MR. LERNER: Your Honor, we can put in the record right now that and we can mark it for the purpose of the record, as Defendant's Exhibit, whatever it is, the latest documents so that the record will be met.

THE COURT: AT all events, this document is -- would be considered a pre August 23rd, '74 edition?

MR. GOIDEL: That's correct, your Honor.

MR. GARMANSKY: I think it would be fair to state that this was the only document put out by Futuristic at a period of time. Would that be true, Mr. Goidel?

MR. GOIDEL: No, that is not fair, because contemplating a change of the law of the State of New York, your Honor, frankly not anticipating anything with regard to the Federal Court proceeding in New York, but anticipating the change of law, Blue Sky Law of the State of New York, which was to go into effect on September 1st, rather, had already been made to revamp the organization of Futuristic Foods and to place people on employment

and so on and so forth.

I don't know that the brochure had actually physically been completed in the sense of being fully printed at that time or whether it was in the hands of the printer, but certainly as of the 23rd, or 24th, they were already being circulated.

Even in -- prior to September 1st. We moved up the date because of the fact the Judge Connors wished me to hold monies in escrow and frankly I preferred not having to hold anything in escrow and so I induced my clients to start the new program even faster. So we would minimize the amount of money that I had to hold.

THE COURT: Your wallet isn't that big?

MR. GOIDEL: Not that big, your Honor.

BY MR. GARMANSKY:

Q Mr. Shevack, do you know Mr. Donald Kirsch?

A Yes.

Q Is he part of Futuristic?

A Yes.

Q What is his position?

A He's vice president of administration.

Q I see. Do you know how Mr. Kirsch became associated with Futuristic?

A Yes.

Q Would you please tell us how that occurred?

A I met Mr. Kirsch in Galaxy Foods and I felt he was intelligent, hard working. I mean, I could stand here, it would sound like a boy scout oath. He worked day and night, trying to set up that retail operation. And when I left Galaxy Foods, that was the one individual that stuck in my gut because you know, like he also left and you know, I felt at that time, like it was all downhill from there on in. He was the only guy I felt that really knew what was going on.

Q Would you like to now answer our question and say how Mr. Kirsch became associated with Futuristic?

Q Mr. William Reichert was friendly with Mr. Donald Kirsch. He found him four, maybe five years before that. I believe that is the proper information. And he invited Mr. Kirsch down to a conference that myself, Mr. Kirsch, Mr. Reichert and one or two other individuals whom we had personally known and we discussed that we had just formed Futuristic Foods Inc. and would they desire to become a part at this time.

Q So you didn't know Mr. Kirsch was coming down? You didn't invite him down, did you?

A No. I knew he was coming but I didn't invite

him, no.

Q You didn't invite him and you were not the first one to generally ask if he wished to be associated with Futuristic, is that correct?

A That's correct.

Q When was this, Mr. Shevack?

A I believe it was in January. No, no. Excuse me. We had a conversation, the beginning of February, if I recall properly.

THE COURT: Now, this conference is in February?

A Yes. The conference -- we were speaking between ourselves in January. We didn't speak to anybody else about it until February, the beginning of February.

Q You had this conference at the beginning of February?

A With Mr. Kirsch, yes. We spoke to him individually in February. Beginning of February.

Q What do you mean by individually? I thought you had a conference? All of you were together.

A We were, but meaning nobody else actually was there. There were four of us there.

MR. GOIDEL: He means on a face to face basis with Mr. Kirsch, I think is what he means.

MR. GARMANSKY: No further question.

MR. GOIDEL: Your Honor, I just would like to take two minutes to clear up just one or two, I think, minor points.

THE COURT: All right. I think the latest arrival can last for two minutes.

Pic fls.

REDIRECT EXAMINATION

BY MR. GOIDEL:

Q Sir, there is a little bit of confusion. I confess in my mind after listening as relates to this McLean matter. Was there any difference of opinion between you and Mr. McLean as to the amount of money to be realized by him when he sold a franchise prior to the time that he was able to put up the $2,000?

A Yes.

Q What was the difference? What did you believe and what did he believe?

A He believed he should earn $500.

MR.LERNER: Objection unless he has a discussion.

THE WITNESS: I did have a discussion.

MR. LERNER: You will have to bring it out.

Q Did you have a discussion?

A Yes.

THE COURT: You should try as best you can to reconstruct the discussion and not make the record appear that you are giving your mental impressions and conclusions. I am supposed to decide what those are based on what was said between the two of you and others.

THE WITNESS: O.K.

THE COURT: First of all, are we talking about some specific time, place, and persons present, if any?

THE WITNESS: Yes.

THE COURT: What is the time?

THE WITNESS: The time is approximately 3 o'clock in the afternoon on a Sunday, in Frank Quack's office, Vice President of Galaxy. We were in his office.

THE COURT: His office was where?

THE WITNESS: In the 303 Stanley Avenue location.

THE COURT: The warehouse?

THE WITNESS: Yes.

THE COURT: When?

THE WITNESS: This was on a Sunday afternoon.

THE COURT: The date, when?

A (No response.)

THE COURT: Approximately?

THE WITNESS: It should have been the same date Mr. McLean's franchise was registered. It should have been. I don't know if it was.

THE COURT: You mean based on the date of the contract?

THE WITNESS: October 8th. Is that a Sunday? If that is a Sunday.

THE COURT: On or about that date?

THE WITNESS: Yes.

Now, Mr. Katz was present and Mr. McLean was present. They had a discussion. At that point Mr. McLean after having that discussion came to me relating the discussion he had and he also discussed with me where I now found out the difference in our opinions was on the amount he was supposed to earn on each person joining the firm that he sponsored in.

I explained to Mr. McLean the way I had explained it to him previously and he still felt I was incorrect for he believed something different was said to him at the other time.

We proceeded back in Mr. Katz' or Mr. Quack's office, where we had a discussions with Bruce Katz, Melvin McLean and myself.

Mr. McLean felt he should be entitled as he was saying to Mr. Katz while I was there, to a $500 commission for every person that joined Galaxy Foods that he recommended.

I explained to Mr. Katz as I had explained to Mr. McLean previously, if an individual invests $2,000 to purchase a field manager's position in that respect he would be entitled to $500. Being he did not invest

the $2,000 necessary to earn the $500, I was offering Mr. McLean a proportional investment.

In other words, if he had invested half the franchise price of $2,000, he would be entitled to half the commission price of $500 or $250.

Now, I would take that $250 and add it to his deposit amount. I would then take the percentage of the $2,000 that had accumulated to -- if it was 40 percent, he would be entitled to 40 percent of the commission of $500.

Mr. Katz explained Mr. McLean was confused about it. He explained to me Mr. McLean didn't feel it was fair.

Now, I never said that is the exact same procedure I joined with. Mr. Lee gave me the full commission which I admit to. But Mr. Lieberman doesn't drive as hard a bargain as I do because I am a more, what I feel, better businessman. I was able to realize a greater profit. It doesn't mean I did anything wrong.

THE COURT: Anyway, however, you were overruled, is that the point?

THE WITNESS: Well, I came to an agreement with Mr. Katz. I could have protested but I felt it would jeopardize my franchise because Mr. Katz felt that he

should be entitled to $500, although I was supposed to be an independent, he almost demanded that I see it his way so I agreed not to make any waves.

BY MR. GOIDEL:

Q I show you this document which is Plaintiff's 43.

THE COURT: Is that in evidence?

MR. GOIDEL: Yes.

Q That is the loan application shown to you just a few minutes ago.

THE COURT: For whom?

MR. GOIDEL: Pardon?

THE COURT: For whom?

THE WITNESS: Mr. Simmons, it says.

MR. GOIDEL: Mr. Simmons.

THE CLERK: That is for Identification, 43.

THE COURT: I thought they agreed it is in Evidence.

MR. GARMANSKY: It is in Evidence.

THE CLERK: It wasn't marked.

Q I will ask you, does there appear on this document any handwriting of yours?

A No.

Q Front, sir, or back?

A No.

MR. GOIDEL: I have no further questions of the witness, your Honor.

THE CLERK: May I have it to mark it in Evidence, your Honor?

MR. GOIDEL: Your Honor, again without the necessity -- I'm sorry. The defendant rests.

THE COURT: All right.

MR. GOIDEL: Your Honor, without making any speeches, I would like to make a few motions. Shall I make them for the record?

THE COURT: Yes. Although I should like to ask the Commission, do you propose to introduce any further evidence on a rebuttal case or anything of that sort?

MR. LERNER: No, we do not.

THE COURT: All right. You may make motions.

MR. GOIDEL: Your Honor, at this time I move to dismiss the complaint on the ground that a prima facie case has not been established. Also on the ground by the preponderance of the credible evidence, the plaintiff has failed to make out a case.

Also, your Honor, your Honor will recall earlier in this matter the motion was made questioning the jurisdiction of the Court. Without going into the

argument I once again renew that motion.

Also I question the jurisdiction of this Court over the person of the defendant Shevack and the defendant Kirsch.

More explicitly, that will be set forth in our argument in a brief to be submitted to your Honor. All of those grounds, we so move.

MR. LERNER: What is the personal jurisdiction problem?

MR. GOIDEL: What is the personal jurisdiction problem?

MR. LERNER: I don't think it has been raised before.

MR. GOIDEL: I am sorry. I meant jurisdiction over the subject matter as relates to the person of the defendant Kirsch and Shevack. That's what I meant.

THE COURT: All right.

MR. GOIDEL: We will of course outline our arguments in a memorandum of law.

THE COURT: When will we expect this illumination?

MR. GOIDEL: I must request several weeks. I am going right on trying another case on Tuesday. Your Honor knows Judge Ward is waiting for me as soon

8 as I get out of that case.

THE COURT: Let me ask counsel for the Commission what they think will be a fair time to deliver a post-trial brief to the Court on the basis of their view of the evidence.

MR. GOIDEL: There are 2,000 pages.

THE COURT: 2,000 pages of testimony. How much time do you want?

MR. LERNER: Thirty days, your Honor.

THE COURT: Thirty days. Including Mr. Garmansky's vacation.

MR. LERNER: Forty-five days, your Honor.

THE COURT: That's it.

THE CLERK: Today is the 10th, your Honor.

THE COURT: Roughly six weeks. Suppose we say November 25th.

MR. LERNER: Right before Thanksgiving.

THE COURT: How about you, are you going to be able to meet that?

MR. GOIDEL: I will certainly endeavor to comply. If I can't, I will give prompt notification to the Court. I can't envision any reason for not being able to.

THE COURT: I know sometimes it's considered desirable to have the briefs come in at the same time.

I don't always find that is so after the case has been tried, to tell you the truth. The Commission will unquestionably focus on the evidence as it sees it, which leads to the result it thinks the case ought to lead to. My own feeling is it leaves the defendant somewhat in the dark and me to the extent the defendant is in the dark, and I would prefer to give him two weeks to deal with your brief. Two weeks beyond that. I assume in the interim he will be marshalling the evidence.

Nevertheless, I think it would help if I have your brief and his in effect responding brief with an opportunity to you to reply to anything he raises there.

MR. LERNER: The only thing I can add is we filed a brief on the preliminary injunction.

THE COURT: I understand that. Let me put it this way, if you want to consider that filing as your statement of the applicable law, I don't see why we have to do it all over again.

MR. LERNER: We would just want to update it and add some additional sections.

THE COURT: I don't want you to hand me a telephone book.

MR. LERNER: Fine.

10 THE COURT: I am more interested in what you say the evidence has shown here on the issues that have been dealt with. At the same time, I think it would be better two weeks after the 25th of November that I receive your answering brief. Then I will give you, if you need, two weeks beyond that.

MR. LERNER: If the Court is willing to accept our additional brief and we would incorporate it into our final brief --

THE COURT: That means November 25th for the Commission's post-trial brief and December 9th for your post-trial brief.

MR. GOIDEL: Yes.

THE COURT: You can have until the 23rd for any reply brief you deem necessary.

MR. LERNER: I understand the findings will be exchanged on the 25th?

THE COURT: Do you wish to do that?

MR. GOIDEL: Frankly, both sides should do it with their respective briefs.

THE COURT: I think you should exchange the findings of facts if you are going to work up a separate set of findings of fact. Those should be exchanged.

MR. GOIDEL: O.K.

THE COURT: On the 25th.

11

MR. GOIDEL: Fine.

THE COURT: Decision reserved on all motions.

MR. LERNER: Thank you, your Honor.

MR. GOIDEL: Thank you, your Honor.

(Whereupon, the proceedings were concluded.)

* * *

PLAINTIFF'S FINDINGS OF FACT AND CONCLUSIONS OF LAW.

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

SECURITIES AND EXCHANGE COMMISSION Plaintiff, -against- GALAXY FOODS, INC. ARTHUR LIEBERMAN a/k/a ARTY LEE RALPH AVNI CHARLES HOROWITZ BRUCE KATZ STEVEN ROTH MARK GLAZER IRWIN DONALD KIRSCHENBLATT a/k/a DONALD KIRSCH GEORGE PADILLA ARTHUR SHEVACK Defendants.	73 Civil Action File No. 1742 FINDINGS OF FACT AND CONCLUSIONS OF LAW PURSUANT TO FEDERAL RULES OF CIVIL PROCEDURE 52

PRELIMINARY STATEMENT

On November 26, 1973, the Securities and Exchange Commission ("Commission"), filed its complaint and other moving papers against the various defendants seeking preliminary and permanent injunctive relief in addition to requiring the defendants to disgorge illegally obtained monies from Galaxy Foods, Inc. ("Galaxy"), and a Temporary Restraining Order prohibiting the waste or dissipation of Galaxy's remaining assets (then a bankrupt under Chapter XI) by any of the defendants.

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PLAINTIFF'S FINDINGS OF FACT AND CONCLUSIONS OF LAW

In January, 1974 all defendants consented to preliminary injunctions. Subsequent thereto, applications were made on behalf of several of the defendants to dismiss the Commission's complaint upon the grounds that the Court did not have jurisdiction over the subject matter of the Complaint (i.e., that a "security" or "investment contract" was involved). On February 12, 1974, the Court dismissed the defendants' motion and ordered the action be set down for plenary trial.

The trial in this matter commenced before Honorable Edward R. Neaher on September 30, 1974 and terminated on October 10, 1974. Prior to and during the trial, Consent Judgments of Permanent Injunction were received from all defendants with the exception of Arthur Shevack and Donald Kirschenblatt. Consequently, with respect to these individuals, the Commission respectfully submits the following Findings of Fact 1/ and Conclusions of Law and respectfully requests they be adopted by the Court.

1/ Hereinafter the Commission's papers will contain the following abreviations: Findings of Fact - F.F.; Transcript - T; Exhibit - Exh.; Plaintiff - Pl.; Defendant - Def.. It should be noted that Plaintiff's Exhibits run from 1 - 44 and Defendants Exhibits from A-N.

PLAINTIFF'S FINDINGS OF FACT AND CONCLUSIONS OF LAW

FINDINGS OF FACT

I. GALAXY FOODS, INC.

A. Description and Background of Galaxy Foods, Inc.

1. Galaxy Foods, Inc. ("Galaxy"), was incorporated in the state of New York on September 2, 1971 for the primary purpose of providing a free home delivery service to consumers of supermarket items. Galaxy had its principal business office at 1864 Flatbush Avenue, Brooklyn, New York. In addition, Galaxy had a warehouse and other offices at 303 Stanley Avenue, Brooklyn, New York. (Def.'s Ex. J; T. 264, 293).

2. Galaxy filed a voluntary petition for bankruptcy in the United States District Court of the Eastern District of New York on November 28, 1973. Its liabilities were listed as approximately $200,000 and its assets were listed as approximately $30,000. (Def.'s Notice of Motion to Dissolve Temporary Restraining Order, Exh. A - Bankruptcy Filing).

3. No registration statement has ever been filed by Galaxy with the Commission as required

by the federal securities laws in order to offer for sale and sell the investment interests described herein. (Pl.'s Exh. 1)

4. The incorporators of Galaxy were Arthur Lieberman ("Lee"), Ralph Avni ("Avni"), and Kenneth Rosenthal ("Rosenthal"). These individuals owned all the 100 outstanding shares of Galaxy common stock in approximately equal amounts, for which stock they contributed a total capital of only approximately $100 to Galaxy. (Def.'s Exh. J, T. 264 - 265).

5. The basic concept and design of the Galaxy operation was derived from a company known as Koscot Interplanetary, Inc. ("Koscot"). Specifically, the methodology of sales techniques, training sessions and investor meetings all were born from the Koscot experience. However, the most stunning similarity between the companies was the earning structure. As in Galaxy, a Koscot investor could earn money in two ways: through the sale of Koscot's retail product or through the recruitment of other investors into the company. (T. 266, 277, 279-280).

6. Not only was the design of Galaxy adopted from Koscot, but the central core of Galaxy's management and supervisory personnel was staffed (approximately 16 in all) with former Koscot people. In fact, the reason for such staffing was to utilize the specific talents and abilities of salesmanship learned at Koscot which would be necessary to get Galaxy on the move as quickly as possible toward the sale of franchises. (T. 278-279).

7. Lee, Avni and Rosenthal first met each other in Koscot, where they owned investment interests. Included among the 16 former Koscot investors recruited by Lee, Avni and Rosenthal was Irwin Donald Kirschenblatt ("Kirsch"), also a Koscot investor, who assumed an executive and supervisory position in Galaxy, see F.F. 21 to 26, and 110, infra. (T. 31, 277-279).

8. In Koscot, Lee attained the position of Assistant State Director of Wholesale for New York, Borough of Manhattan, which entitled him to a percentage of all gross sales of Koscot

investment interests in Manhattan. Lee became acquainted at that time with Arthur Shevack ("Shevack"), a Koscot investor of similar position in Koscot, Assistant State Director of Wholesale for New York, Borough of Brooklyn, and became acquainted with Shevack's special sales ability and command of sales techniques essential in the sale of investments interests. Lee attempted to recruit Shevack at the same time as the other Koscot members referred to in F.F. 6 and 7, supra, in the summer of 1971, but Shevack did not join Galaxy until a later time. (T. 277, 349, 396-398, 1470-1474, 1515-1517, 1535-1537).

9. In approximately June, 1972, Shevack met Lee in Brooklyn at which time Lee personally renewed the invitation to join Galaxy referred to in F.F. 8, supra. Lee extended Shevack a "special deal" whereby he (Shevack) could work his way into Galaxy in exchange for an investment interest, working directly for Lee. Lee agreed to give Shevack all commissions to be earned for each investor Shevack sponsored into Galaxy with the understanding that when Shevack had received $5,000 in commissions he would

purchase his own Distributor investment. Subsequent thereto, Shevack would continue to secure new investors using the sales techniques he had developed successfully in Koscot, and earn commissions in Shevack's own name. See F.F. 71 and 72, infra. (T. 396-398, 1469-1471).

B. Business Purpose and Operations of Galaxy

10. Galaxy was purportedly incorporated for the primary purpose of providing a free home delivery service to consumers of supermarket items which the consumer would purchase from Galaxy at competitive retail prices. However, in order to raise the needed capital to implement the retail food program, Galaxy, in September, 1971, commenced offering and selling "franchises" or investment interests in Galaxy to the public. Galaxy itself described the interests that it was offering for sale and selling as investments. (T. 265, 281, Pl.'s Exh. 3, 4, 5, 6, 7, 8, 14, 14A, 15, 16, Def.'s Exh. G, J).

11. Galaxy offered for sale two types of investments. The first was called the Field Manager position ("Manager"). The Manager interest

initially sold for $1,000, but changed to $2,000 in March, 1972, and then to $3,000 in October, 1972. The offer or sale of Manager positions ceased after August, 1973. The second type of investment offered to the public was called a Distributorship position ("Distributor"). The Distributor position initially sold for $3,000, but was also raised to $5,000 in March, 1972, and to $7,000 in October, 1972. (Pl.'s Exh. 3, Part II pp. 1 - 5, Pl.'s Exh. 4, Part II pp. 1 - 5, Pl.'s Exh. 5, Part II, pp. 1 - 4, Pl's Exh. 25 p. 10, T. 280-281).

12. If an individual invested in the Manager position, he would receive the following: training provided by Galaxy in all its business aspects; training for all the sales personnel he recruits for his own sales organization; a commission of $750 (or $300 or $500 depending on the price of the investment at the time) for sponsoring a new Manager or Distributor into Galaxy; a 10% commission on all initial food Orders; a 3% commission on all re-orders of food. A Manager, if sponsored into Galaxy by a Distributor, is considered as part of the

sponsoring Distributor's organization. (Pl.'s Exh. 3, Part II, p. 2, Pl.'s Exh. 5, Part II, p. 2, Pl.'s Exh. 4, Part II, p. 2, T. 280-281).

13. For his investment in a Distributor position a investor would receive training in all business aspects of Galaxy; eligibility for executive business management training; eligibility for a company position; a commission of $1,050 (or $400 or $750 depending on the price of the investment at the time) when he sponsors a Manager into Galaxy and an additional commission of $1,400 (or $850 or $1,250 depending on the price of the investment at the time) if that Manager elevates to a Distributor investment; a commission of $350 (or $100 or $250) when a Manager, recruited by the Distributor, in turn recruits another Manager, and an additional $1,400 (or $850 or $1,250) if the new Manager becomes a Distributor; a commission of $2,450 (or $1,250 or $1,950 depending on the price of the investment at the time) when a Distributor sponsors another Distributor into Galaxy; a 15% commission on all initial retail orders and a 5% commission on all re-order volume from his personally

acquired accounts; 5% override commission on initial retail order volume of his Manager; and a 2% override commission on retain re-orders from Managers in his organization. (Pl.'s Exh. 3, Part II, p. 4, Pl.'s Exh. 4, Part II, p. 4; Pl.'s Exh. 5, Part II, p. 4; T. 280-281).

14. Galaxy at no time commenced a full-scale retail program. The only retail delivery was a limited delivery area "pilot program", which did not commence until the end of November, 1972, and lasted for only approximately four months. (Pl.'s Exh. 25 p. 4, p. 12)

15. Even though Galaxy described its wholesale operations, i.e., the sale of Manager and Distributor interests, as a way to earn money for "a limited time," the entire thrust and primary emphasis of Galaxy was geared to the business aspect of persuading new investors to join Galaxy. This is demonstrated by the fact that the sale of investments was the only source of income earned by Galaxy from its incorporation until its demise, a period of over two years, except for the "pilot programs" retail sales, referred to in F.F. 14, supra. (Pl.'s Exh. 11, 25 p. 3, p. 8-9, T. 296).

16. That the primary emphasis of Galaxy's operations was on wholesale investment sales is also obvious from the individual investor's point of view. It is clear that an investor could earn much more money selling Manager and Distributor positions instead of obtaining customers for food orders. In fact, an investor in Galaxy who obtained customers to order food during the "pilot program" was told that he would not even receive the commissions he was entitled to receive. (This position was later modified so that some restricted retail commissions were paid in approximately March, 1973. One such investor, Melvin McLean, was told by a member of Galaxy's management that he would not be able to receive commissions for any of his retail customers because their total orders did not exceed $750, a fact unknown to Melvin McLean when he joined.) Therefore, the only way an investor could earn money in Galaxy was by sponsoring new individuals into Galaxy. As a consequence of the restrictions on retail commissions, the money that should have gone to the investor for his retail sales during the "pilot program" instead went into the pockets of the Galaxy management. Additionally, it also behooved

Galaxy's management to emphasize wholesaling because the management individuals received a percentage of all gross sales of Manager and Distributor positions. (T. 39, 282-283, 291-293, 1255-1257, 1271, 1318-19, Pl.'s Exh. 3, 4, 5, 6, 22, 25 p. 8).

17. The obligation of Galaxy to pay commissions on retail food sales was vitiated by the limitation that commissions would not be paid until a total of 8,000 to 10,000 customers were secured to order food under the Galaxy delivery program, defined by management as a "full retail program." The probability that this contingency would never occur is obvious from the fact that after more than one year of business operations, Galaxy had accumulated only approximately 1,400 customers. Galaxy had combed the designated delivery radius around the warehouse to secure these customers, and there was little likelihood that individual investors would have any greater success. (Pl.'s Exh. 3, 4, 5, 23, T. 345, 1461-1462).

18. Analyzing the breakdown of every dollar ($1.00) that came into Galaxy from the sale of investment

interests, it becomes quite clear that Galaxy was not properly funding the establishment of a retail food program of the magnitude claimed in promotional literature. From every one dollar ($1.00) received by Galaxy approximately fifty-eight cents ($.58) was taken out automatically in the following amounts:

(1) Thirty-five cents ($.35) to forty cents ($.40) for commission fees to a sponsoring investor, and

(2) Eighteen cents ($.18) as override commissions to Galaxy's management.

The remaining forty-two cents ($.42) was to be used for the food program to cover all expenses including warehouse and business office rental expense, leasing of trucks, purchase of food, salary to employees, leasing of a computer, conveyor belts, and many other material items needed to set up a food sale and delivery program. (T. 285, 294-296).

19. Between approximately September, 1971 and approximately September, 1973, Galaxy sold in excess of 800 investments to the public comprising Distributor and Manager positions.

Galaxy and the defendants raised in excess of $2,400,000 from the sale of these investments. (Def.'s Exh. G).

C. Management Organization and Structure of Galaxy

20. The management of Galaxy was divided into separate divisions - the Board of Directors and the Executive Board. The Board of Directors was initially comprised of Lee, Avni, and Rosenthal until June, 1972, the date of Rosenthal's leaving the corporation, when Charles Horowitz ("Horowitz") became a director. Each member of the Board of Directors received from 3% to 4% commission on the gross sales of Manager and Distributor positions. The duties and responsibilities of the Board of Directors were to oversee the functioning of the operating arm of Galaxy which was the Executive Board. In fact, the Board of Directors delegated the entire business operations to the Executive Board although retaining the right to veto any decision or action by the Executive Board.

In addition, the members of the Board of Directors held certain corporate positions in Galaxy as follows: From September, 1971 to June, 1972, Lee was secretary-treasurer, Avni

was vice-president and Rosenthal was president. In June, 1972, with Rosenthal's resignation, Lee stayed as secretary-treasurer, Avni became president, and Horowitz became vice-president. (Pl.'s Exh. 11, Def.'s Exh. G, T. 272, 275, 282-85, 291, 293, 444-47, 455-459).

21. The Executive Board of Galaxy was comprised of the three members of the Board of Directors (referred to in F.F. 20, supra), a president of the Executive Board, and five Executive Vice-Presidents. From approximately September, 1971 to January, 1973, the members of the Executive Board, excluding the Board of Directors, were: John Celano ("Celano"), Executive Vice-President of Administration; Stevens Roth ("Roth") Executive Vice-President of Field Manager Operations; Thomas Rosenthal ("Rosenthal") Executive Vice-President of Transportation; Hirsch, Executive Vice-President of Marketing; Franz Quack ("Quack") Executive Vice-President of Warehousing; and Bruce Katz ("Katz"), President of the Executive Board. (T. 31-33 239-40, 272-74, Pl.'s Exh. 11).

22. The Executive Board had complete responsibility to organize and control all policy and business

aspects of Galaxy. The Executive Board exercised a myriad of functions including the following: implementing specific formats to be followed at Galaxy meetings for potential investors and sales tactics to procure new investment; the agenda and content of courses to be taught at Galaxy training sessions; the placement of Galaxy advertisements in newspapers concerning retail and wholesale; providing speakers from the Executive Board at Galaxy meetings for new investors; proposing budgets and expenditures of funds; discussing and entering into contracts and leases; preparing and distributing literature, brochures and other documents to existing investors concerning the present and future business status of Galaxy in both wholesale and retail; and providing leadership and the motivation to all Galaxy investors. Kirsch was present at the Executive Board meetings where all of the foregoing policy decisions were discussed and made. (T. 272, 275, 315-316, 324-325, 328-329, 333-335, 357-361, 446-447, 833-835, Pl.'s Exh. 8, 13, 13A, 13B, 13C).

23. Certain executives of Galaxy, including Lee, Avni, Katz, Morowitz, Kirsch and others were awarded a Distributor investment free of charge or for services. (T. 36, 201-202, 202, 421).

24. Kirsch, as Executive Vice-President of Marketing, not only participated in Executive Board meetings described in F.F. 22, supra, but also directed, supervised and had responsibility for the preparation of the Galaxy food catalog, the sales arrangements with respect to the purchase of food and the complete stocking of the Galaxy warehouse. Additional duties included supervision of employees, ultimately approximately fourteen employees, in his department. He functioned as a full-time officer, the marketing expert available to other managers and investors alike to answer all questions about retailing and the marketing aspect of the business. Kirsch identified himself as, and acknowledged himself to be, an "officer" of Galaxy. (T. 206-207, 275, 277, 450-451, Kirsch Affidavit of November 3 (sic), 1973).

25. Kirsch participated in other management functions directly related to the business

operations of Galaxy. He served as an instructor in business training at training sessions, described infra. Kirsch attended between 50 and 75 Opportunity Meetings, described infra, during his association with Galaxy, where he was identified to investors by title, Vice-President of Marketing and as a member of the Executive Board, during question and answer periods. He gave a presentation speech at one Opportunity Meeting. As a member of the Executive Board of Galaxy, Kirsch was obligated to be present at all Sunday Step-Up Meetings held by Galaxy, described infra. At both types of meetings, Kirsch was observed to assist in the task of persuading persons to invest in Galaxy, which was an effort expected of all executives. Lee would also on occasion take investors into Kirsch's Galaxy offices for his explanation of business operations or marketing. Kirsch performed the foregoing functions until he resigned from his Galaxy office in January, 1973, effective February 1, 1973. (T. 49-51, 61, 81, 87, 203-205, 421-422, 834-835, Pl.'s Exh. 25 p. 6, Def.'s Exh. E)

26. From approximately September, 1971 through January, 1973 defendant Kirsch earned approximately $18,000 from Galaxy which represented commission's amounting to one-half of one percent to one percent of the total sales of investments sold during this period. He also earned in that same period commissions from his sponsoring of three individuals into Galaxy. (T. 44-45, 282, 284, 291, 293, 465-466, Def.'s Exh. G).

D. Offers and Sales of Manager and Distributor Positions to Investors outside of New York State

27. At least two investment positions in Galaxy were offered and sold to individuals who resided outside of New York State and who were known to be non-residents of New York State by the Galaxy management who approved and processed their applications to invest in Galaxy. (Pl.'s Exh. 20, 29, 30, T. 792, 1035).

28. Paul Deceglie ("Deceglie") invested in a Manager position in Galaxy in approximately October, 1971. At the time he joined Galaxy he was residing in Mandham, New Jersey. Deceglie

listed his New Jersey address on his application which was approved by a Galaxy executive. (T. 1035, 1041-1042).

29. To further show that the Galaxy management knew Deceglie was residing outside of New York State, Galaxy mailed to him at his New Jersey address numerous bulletins, brochures, and other literature concerning the business operations of Galaxy. In addition, Horowitz, who was President of the Executive Board at this time, called Deceglie at his home in New Jersey in April, 1972 (Deceglie resided in Lake Hiawatha, New Jersey when Horowitz called him). Horowitz acknowledged to Deceglie that Deceglie was a New Jersey resident and Horowitz then told Deceglie that in order to stay in Galaxy he would have to establish a nNew York State residency (Horowitz told Deceglie a "mailing address" would be sufficient) or that Deceglie could receive back his initial investment in Galaxy if he chose to do so. (T. 1055-1056, 1087-1090).

30. Deceglie opted to receive back his investment in Galaxy, and he terminated his association with Galaxy on or about May 3, 1972 after spending approximately seven months in the organization. The check stub receipt given to Deceglie for his refund states that the refund is being made to ". . . manager residing outside of New York State." (Pl.'s Exh. 30, T. 1038).

31. Werner Kunst ("Kunst"), who resided at Wurmkamp 1, Hamburg - Schenefeld, Germany, mailing address c/o F. Quack, 565 - 9th Street, Brooklyn, New York 11215, listed his Germany address on his application for a Manager position when he decided to invest in Galaxy in February, 1972. Attached to Kunst's application were a copy of a check evidencing his purchase of a Manager investment, an approval form for the investment, an elevation form and an agreement which acknowledged that Kunst is a resident of Hamburg, Germany, signed by the then Chairman of the Board of Galaxy, Rosenthal. (Pl.'s Exh. 20, T. 792-793, 795-796, 802).

II. GALAXY MEETINGS AS PRINCIPAL SELLING EFFORTS

E. Opportunity Meetings

32. The principal selling effort of Manager and Distributor participation interests by Galaxy occurs at promotion meetings of two types. The first type, Opportunity Meetings, were held three - four times per week from approximately September, 1971 through August, 1973. They were attended by the Galaxy management and existing investors in Galaxy who bring to the meetings their invited "guests" or "prospects". The Opportunity Meetings were designed, organized, controlled and run by the Galaxy management. The existing investor had no control or voice concerning the format of the meetings or the content of the speeches, apart from a question and answer period at the end of the formal speeches when questions of potential investors were directed at speakers and members of the Executive Board, including Kirsch. The Opportunity Meeting was divided into four parts with four different speakers and the last speaker was a "guest speaker" who was always a member of the Galaxy management. (Pl.'s Ex. 3, 4, 5, 6, T. 297-298, 305-309, 896).

33. Opportunity Meetings were conducted with a forceful appearance of great enthusiasm and motivational spontaneity. The speakers, including members of the Galaxy executives, spoke quickly, loudly and with great emotion and conviction. The speakers, however, follow a strict, memorized script prepared by the Galaxy management. The speakers were not permitted to deviate from the script at all except for the guest speaker, a member of Galaxy's management. (Pl's. Exh. 3, 4, 5, 6, T. 305-308, 921, 1038-39).

34. At the Opportunity Meetings, the atmosphere created by the defendants was one of high pressure tactics set against a background of glamorized, carnival type machinations. These machinations and devices included enthusiastic responses of cheering, applauding, running up and down the aisles and verbal outbursts, notably the "Money-Hum," where the audience chants in unison "M-M-M- Money!" The cheering and applauding has been observed to commence with the Galaxy management, employees

and existing investors. Galaxy management held out to the guests the prospect of overwhelming financial success to be achieved by anyone investing in Galaxy which was highly dramatized by the use of a blackboard upon which various amounts of money were written including the figure of $60,000 in large numbers, constantly repeated throughout the meeting amid cheering and applauding, which is the amount prospective investors were told they can earn with Galaxy in a single year. Investors who respond to the imagined stampede to great riches and announce they will invest in Galaxy were also hailed with outbursts of cheering and applause. (T. 90-91, 310-312, 320-321, 894-896, 1025, 1028-1030, 1111-1115, 1214-1218, 1309, 1436-1437)

35. The illusion of great wealth and potential financial return was emphasized by the speakers with skillful reference to expensive cars, fashionably dressed investors and stories of great riches achieved through Galaxy. The script followed by defendants' speakers carefully avoids actually guaranteeing a return and does contain a

statement that the prospect must expect to work. The impression which is fostered, however, by emphasis and psychological technique, is on the near inevitability of success achieved by anyone who follows the defendant's directions. This is illustrated in the description of Galaxy in the business manuals given to each investor, which contains the script of Opportunity Meetings, a description of Manager and Distributor investments and rules and regulations. Galaxy is described in the business manuals as a ". . . program where the average distributor may earn great sums of money . . .;" ". . . a proven venicle of success and the marketing plan we will be discussing has been used successfully to make men and women thousands, even millions of dollars." (Emphasis in original) (Pl's. Exh. 3, 4, and 5 Part II, p. 1; Pl.'s Exh. 3, 4, 5, and 6, introduction; Pl.'s Exh. 3 and 4, p. 2; Pl.'s Exh. 5 and 6, p. 1).

36. The applause, cheers and chants described in F.F. 34, supra were formulated as management sales tools or psychological techniques to put prospective investors in an enthusiastic frame of mind or emotional ferver conducive to

persuading the potential investor to join Galaxy. The primary purpose of conducting Opportunity Meetings as described in F.F. 32 to 35, supra was calculated to completely indoctrinate the potential investor with illusions and dreams of fantastic riches that were obtainable only through a Galaxy investment while preventing the potential investor from using a dispassionate, critical eye in evaluating the merits of such investment. (T. 297, 310-319).

F. Sunday Step-Up Meetings

37. Propsects who have not succumbed at the "Opportunity Meetings" are invited to attend the "Sunday Step-Up Meeting," initially held at Galaxy management offices and later at the Galaxy warehouse. These meetings were held once a week on Sunday from approximately September, 1971 through August, 1973. The formal presentation follows a tour of the Galaxy warehouse. At these meetings there was usually only one speaker, always from Galaxy's management, who again emphasized the huge benefits to be derived by investing in the Galaxy promotion. Again, the

same psychological techniques, enthusiastic responses and illusions of affluence used at the "Opportunity Meetings" were employed at "Sunday Step-Up Meetings" in order to induce potential investors into Galaxy. As an additional psychological effect, the speaker would stage a dramatic presentation of checks called "Payday." He would hand out checks to existing investors purporting to represent their share of commissions earned from the investments of persons they have introduced into Galaxy. (Checks for retail sales, issued only in March or April, 1973 were not dispensed at meetings in this fashion.) The speaker would call a prospect or potential investor to the front of the room to call off the name and amount of money on each check to prove to the potential investors that the checks are real. This is accompanied by loud cheering and applauding. The successful investor is asked by the speaker to tell his success story, which is then heralded as the success of an ordinary person who had joined Galaxy a short time ago. The use of this Payday device was approved by the Galaxy Executive Board to demonstrate the amount of money which could be earned from the sale of investments.

The high visibility and tangible reality of checks paid to ordinary investors was designed as an effective sales tool to convince others of the inevitability of their own success if they invested in Galaxy. (T. 297-298, 324, 330-334, 920, 926-927, 1123-1126, 1314-1315).

38. At a point in the meeting the speaker will exclain that he "smells money in the room" or "is there any money in the room?" At this point, several participants hold up checks they have purportedly just received from new investors and bring these checks to the speaker who announces who has just joined Galaxy amid much loud cheering and applauding. (T. 1126)

39. An additional staged device at Sunday Step-Up Meetings was a procedure designed to secure a binding, irrevocable committment to invest in Galaxy. The speaker, a member of the Galaxy management, invites all prospective investors to stand in a line and asks each one to state his name, present occupation, and how they are joining Galaxy, whether as a Manager or Distributor. The form in which the question is posed is a

psychological device designed by management to eliminate the choice of not joining. The entire "closing" procedure, that is, securing a committment from the investor, was formulated to incorporate these psychological sales tools to persuade prospects to purchase investments. The process was calculated to instill in the mind of the prospective investor an unconscious desire to invest in Galaxy because he had already committed himself aloud in front of the whole audience of existing investors and Galaxy management. Furthermore, the dramatic cheering and applauding by the audience of existing investors which accompanied each affirmative response to join Galaxy made by the prospective investors strongly reinforced this unconscious desire and committment to join. (T. 322-330, 920, 1126).

40. From the inception of the Opportunity Meetings and Sunday Step-Up Meetings until the demise of Galaxy, meetings were run in the same manner and followed the same procedures, referred to in F.F. 32 to 39, supra, with the exception that

the enthusiasm, verbal outbursts, cheering and applauding of the investors and Galaxy management grew, creating a wilder atmosphere calculated to ignore or bypass rational objections and analyis and to exert greater pressure on prospective investors to commit themselves to invest in Galaxy. (T. 315-316, 899, 917, 919, 1128, 1129, 1252, 1317).

41. After the conclusion of the Opportunity and Sunday Step-Up Meetings, existing Distributors and Managers, including Shevack, and officers and management officials of Galaxy, including Kirsch, attempted to persuade prospects to invest in one of the positions in Galaxy, with emphasis on the highest position of Distributor. Trained sales agents and the Galaxy management who are specialists in the required techniques of psychological hard-sell, including Shevack and Kirsch, take over and accomplish the closing or sale in the name of the sponsoring individual who gets the commissions for the sale, sometimes without the latter even having been present. (T. 834-835, 397-398, 982-983, 1085-1087, 1174-1175, 1284- 1287).

42. Few, if any, purchasers of these investments have achieved any success remotely approaching that described by the defendants and their agents in meetings or Galaxy literature. (Def.'s Exh. G; Def.'s Exh. R; T. 917-918, 1004, 1151, 1252, 1350).

43. Prospective investors are not informed at any point in the formal presentation speeches of the Opportunity Meetings or Sunday Step-Up Meetings that they must leave the meeting hall if they are not New York residents, or that they cannot make applications to purchase investments, or even that their applications will be refused if they are not bona fide New York residents. Indeed, applications have been approved for non-residents of New York as described in F.F. 27 to 31, supra. (808-810, 903, 1024-1025, 1035).

44. Purported limitation of the Galaxy investment opportunity to New York residents only did not appear in the Galaxy business manuals given to all investors by Galaxy until approximately October, 1972. At that point in time, hundreds of persons, including at least two non-residents, had invested in Galaxy, and an untold number of

indiscriminate offers to join Galaxy had already been made. (Pl.'s Exh. 3, p. 9-10, Pl.'s Exh. 4, 5, 6, Def.'s Exh. G, T. 307-308).

45. The distributor applications and agreements, which were printed in several colors and forms throughout the existence of Galaxy, do not contain a restrictive legend or language which limits the sale of franchises to residents of New York State or residents of one state only. (T. 802-803, Pl.'s Exh. 8, 27, 33, 35).

G. Misstatements of Material Facts in Connection With the Offer and Sale of Investment Interests

46. The Galaxy management approved in Executive Board Meetings the wording and distribution of newspaper advertisements, flyers and invitation cards. These flyers and cards were indiscriminately distributed to the general public, while newspaper advertisements were placed in newspapers of general circulation. The advertisements, flyers and cards misrepresented to prospective investors that an investment in Galaxy was an unqualified "guaranteed investment," i.e., that an investor could receive his money back if he was not totally

satisfied with his investment or wished a refund. (Pl.'s Exh. 7, 14, 14A, 15, 16, 34, T. 774-779, 1119-1120, 1259, 1612-1613).

47. Actually, Galaxy never offered or sold an investment which was "guaranteed". This so-called "guarantee" was, in effect, an obligation to buy-back an investor's Distributor or Manager position if certain events had not occurred by June 30, 1973, including if Galaxy had not begun full-scale retail operations. More importantly, an investor could receive back no more than approximately 50% of his investment in Galaxy. (Pl.'s Exh. 3, Part II, p. 9 (Rule 21), Pl.'s Exh. 4, Part II, p. 9 (Rule 21), Pl.'s Exh. 5, Part II, p. 8 (Rule 21), T. 392-395).

48. Beginning with approximately October, 1972, Galaxy made another promise to investors to assure them they possessed a "guaranteed investment." After Galaxy had been operating a full-scale retail program for at least six months, investors could exercise their "final buy-back option." This promise by Galaxy was limited even more than the buy-back provisions of Rule 21

described in F.F. 47, supra. An investor's "guarantee" was for no more than 50% of the purchase price of his investment, less any amount of commissions earned by that investor for sponsoring others into Galaxy. Of course, six months of retail operations never occurred. (Pl.'s Exh. 3, Part II, p. 10 (Rule 25).

49. Galaxy at no time had the financial capability to honor its "guarantees" to investors of the rights under Rules 21 and 25. In fact, no sinking fund, reserve or other financial provision was inaugurated to insure that Rules 21 and 25 would not be an empty promise. (See F.F. 13, supra)

50. The "guarantees" of Rules 21 and 25, described in F.F. 46-48, supra, were declared null and void by the Galaxy management for all investors joining Galaxy after July 1, 1973. (Pl.'s Exh. 25 p. 10).

51. In seeking to persuade potential investors or prospects to invest in a Galaxy Manager or Distributor position, Galaxy officers, directors,

executives and agents made representations in meetings or in literature distributed by Galaxy management to investors which were not true or accurate when made, including:

(a) That investors who join Galaxy will earn huge profits, as much as $60,000 a year. (T. 310-312, 804-805, 1025, 1028, 1111-1113, 1214-1216, 1309).

(b) That many investors have earned and are earning substantial sums of money in Galaxy. (Pl.'s Exh. 3, 4, 5, 6)

(c) That it would be possible to retire on the money one could earn in Galaxy in little more than one year. (T. 1030)

(d) That Galaxy was operating in Canada and Upstate New York. (Pl.'s Exh. 11, 17, 21, T. 806)

(e) That Galaxy would deliver food items in the Carnarsie area and throughout Brooklyn, or in a thirty-mile radius around the Galaxy warehouse. (Pl.'s Exh. 17, T. 829-830, 923, 1133-1134)

(f) That Galaxy would pay commissions on all sales of retail food. (Pl.'s Exh. 3, 4, 5, Part II; T. 924, 1131, 1213, 1255, 1256, 1303, 1318-1319, 1482)

(g) That Galaxy would acquire and distribute 8,000 to 10,000 customers of the retail program to all Galaxy investors. (Pl.'s Exh. 25 p. 4, 837, 921-922, 1057, 1131)

(h) That Galaxy would commence retail operations on various target dates including January 1972, July 1972, August 1972, September 1972, and October 1972. (T. 243-253, 922-924, 1056-1057, 1121-1122, 1310, 1313, 1482, Pl.'s Exh. 10)

(i) That the Galaxy concept is a proven vehicle for success. (Pl.'s Exh. 3, 4, 5, 6).

H. Omissions of Material Facts in Connection With the Sale of Investment Interests

52. In seeking to persuade potential investors or prospects to invest in Galaxy investments,

Galaxy officers, directors, executives and agents omitted to state material facts or failed to disclose material facts necessary to make the statements made not misleading, which facts were known by them to be true and material, including:

(a) That honorary franchises were awarded to the Galaxy Management including Kirsch for which they did not pay any money. (T. 36, 201-202, 232, 421, 1140)

(b) That the executives of Galaxy, including Kirsch, received commissions on the gross sales of franchises amounting to 18% or $.18 of every $1.00 paid into Galaxy for purchases of investments. (T. 294, 1150-1151, 1253, Def.'s Exh. G)

(c) That commissions were paid to the sponsoring Manager and/or Distributor, as well as to executives of Galaxy, on gross sales of investments amounting to 58% or $.58 of every $1.00 paid into Galaxy for purchases of investments. (T. 285, 294-296, 1150-1151, Def.'s Exh. G)

(d) That no Manager or Distributor actually made $60,000 during a 12 month period of association in Galaxy, from the sale of retail food or investments or both. (Def.'s Exh. G, T. 917-918, 1094, 1151, 1252, 1350)

(e) That Galaxy was patterned directly after Koscot, which was a known pyramid promotion scheme. (T. 278-280)

(f) That most of the investors in Galaxy lose the amounts they have invested. (Def.'s Notice of Motion to Dissolve Temporary Restraining Order, Exh. A, Bankruptcy Filing).

(g) That the Galaxy Management employed numerous, subtle psychological techniques to make a potential purchaser invest in Galaxy. (See F.F. 32 to 41, supra).

III. TRAINING SESSIONS AS INSTRUMENTS OF CONTROL BY THE GALAXY MANAGEMENT OVER TECHNIQUES OF PROSPECTING

53. Training sessions which taught new investors in Galaxy the methods of processing retail sales orders and the methods of earning commissions

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by the sale of new investments were held from approximately October, 1971 through approximately July, 1973, either at the Galaxy executive offices on Flatbush Avenue, Brooklyn, New York at the warehouse facilities on Stanley Avenue, Brooklyn, New York or at various rented halls, from one to four times a month, depending on the demand created by the traffic of new investors. They lasted approximately one week and they were mandatory for new investors. (T. 336, 356-359, 911, 1135, Pl.'s Exh. 3, Part II Rule 23, 8, p. 2, 25 p. 6)

54. Training sessions were expanded and specialized by the Galaxy management to groom potential Galaxy officers and agents, and also to develop the Spanish-speaking investors with Spanish language training sessions. (Pl.'s Exh. 24, 25 p. 7, p. 13, T. 417)

55. All members of the Executive Board, including the defendant Kirsch, served as instructors in the training sessions at some time. Instructors who held no executive position in Galaxy had to be approved by the Galaxy management. (T. 337, 358-359).

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56. The Galaxy management planned, organized, scheduled and designed the training sessions as a critical instrument of psychological brainwashing and indoctrination of new investors. The sessions were inaugurated to limit and control the manner and detail in which the Galaxy operations were described to potential investors by existing investors. The overriding aim of the sessions was to indoctrinate investors in the techniques and methods of enticing and inviting prospective investors to attend Opportunity and Sunday Step-Up Meetings, wherein the Galaxy management then could work effectively to persuade prospects to invest in Galaxy by utilizing the methods described in F.F. 32 to 41 supra. These methods and techniques of finding prospects were known collectively by the term "prospecting," a term of art common to previously successful pyramid sales promotions, such as Koscot. (T. 297, 359-360, 368-369, Pl.'s Exh. 25, p. 6)

57. The format of training sessions typically included:

(a) Discussion of Goals - Why Am I Alive,

(b) Business Training,

(c) Motivation,

(d) Prospecting,

(e) Follow-Up and Step-Up,

(f) Closing Techniques and G-T-C -- Get the Check.

Emphasis was placed on the attitudes, behavior, illusion of affluence and appearance of investors to be displayed in prospecting and at Opportunity and Sunday Step-Up Meetings. (T. 319, 357, 361, 371-372, 383-384, 1135-40, 1254, 1257, 1298-1299, Pl.'s Exh. 12, 25, p. 6)

58. New investors are instructed at training sessions in various forms of prospecting, such as "cold canvassing", which involves approaching strangers in the street to entice them to Opportunity Meetings. Galaxy investors are directed to approach friends and relatives, as well as strangers, greet them in a friendly manner and invite them to an Opportunity Meeting where they can learn how to become rich. Investors are "taught" to seek out prospective investors in Penn Station, Grand Central Station, subway stops, restaurants and on the street - in short, anywhere and everywhere. (T. 361, 910, 912, 1136-1138, 1254)

59. New investors are not instructed to make any attempt to search out persons with sales ability, financial acumen or other skills. They are not instructed to only accost New York residents or to ask the address of a prospect before extending an invitation to a meeting. (T. 921).

60. In order to motivate new investors and to show them precisely how to proceed, the instructors and agents of Galaxy management at training sessions set up simulated encounters between the "typical investor" and the "typical prospect". (T. 910, 1137-1138)

61. Investors are cautioned by the instructors not to give the prospects any specifics about the Galaxy operation or the cost of the investment. They are instructed to disclose just enough to arouse the prospects' curiosity to persuade them to come to an Opportunity Meeting. (T. 362, 366-369, 910, 912-913, 1138-40, 1254).

62. One of the principal methods of arousing curiosity which is emphasized by Galaxy defendants,

agents and instructors is for the investors to make promises of huge profits which can be made each year. Investors are instructed to greet prospects and say "How would you like to make $60,000 a year?" or "How would you like to earn what you are worth not what someone else thinks you are worth?" (T. 366-367, 910, 1136, 1138, 1254)

63. Another prospecting technique is to create an illusion of affluence. Investors were instructed to look and act successful. New investors were instructed to think and act positively and enthusiastically, i.e., "to think and grow rich", when accosting prospects or attending meetings with prospects. At some sessions, Dare to be Great tapes were played. They were instructed to cheer and applaud the speakers and at the mention of money or references to earning $60,000 a year in Galaxy at the meetings. (T. 371, 911, 915-917, 927, 989)

64. Investors were taught to assist a prospective investor in the methods of raising the money to invest in Galaxy, including bank loans, cash value of insurance and loan value of savings

accounts. Investors were also schooled in the "friendly" approach, rendering personal services to prospects such as chauffeuring them to and from meetings or to several banks to get money or loans to invest, or taking prospects out to dinner. At the Opportunity and Sunday Step-Up Meetings, the investor was told to sit with his prospect to allow for the infectious transfer of enthusiasm triggered by the management's speeches. (T. 368, 383-384, 917, 919, 1257, 1290)

IV. THE LIMITED ROLE OF INVESTORS IN GALAXY

65. Investors are taught at training sessions that the ultimate end of all prospecting techniques and training is getting prospects to the meetings. The investor is told that this is of crucial importance because it delivers the prospects into the controlled environment of the Opportunity and Sunday Step-Up Meetings and into the capable, experienced hands of the Galaxy executives who will then secure new investments for Galaxy and commissions for the sponsoring investors. (T. 371, 913, 1086-1087, 1139, 1254)

66. Investors are instructed by Galaxy executives, agents, and instructors that the investors' role is limited strictly to enticing prospects to come to the Opportunity Meetings. (T. 365-366, 1086-1087, 1138-1140)

67. Investors are taught at training sessions to rely on the efforts of the Galaxy management in convincing prospects to invest and as a result of the Galaxy management's efforts at the recruitment meetings, the investor will receive substantial commissions when the prospect he sponsors invests in Galaxy. In terms used by investor witnesses, the investor is taught that the Galaxy management will "get the check" for the investor. (T. 371, 912-913, 1138-1140)

68. The ordinary Galaxy investor who receives only one week of training and does not possess a sophisticated knowledge or understanding of business or sales skills, or even the intricacies of the Galaxy finances and operations, is therefore

forced to rely on the efforts of the organized, experienced Galaxy management to persuade his prospect to invest in Galaxy. In fact, the investor becomes another sales tool to be programmed, controlled, manipulated and used to simply provide prospects for the Galaxy promotional scheme. (T. 368-369, 913)

69. The methods of prospecting taught at training sessions and by Galaxy management and agents were in fact used and employed by Galaxy investors to entice prospects to Opportunity Meetings. (T. 909-910, 1109-1110, 1174-1175, 1208, 1307)

70. The Galaxy investor did in fact rely on the efforts of the Galaxy management in the organized, orchestrated high-pressure sales atmosphere of meetings, and as a result of these essential managerial efforts, prospects were in fact persuaded to invest in Galaxy. As a result of the investment by prospects, commissions were in fact earned by investors who had not contributed the essential primary efforts to procure the investment. (T. 897-898, 1174-1175, 1285-1287)

PLAINTIFF'S FINDINGS OF FACT AND CONCLUSIONS OF LAW

V. PROSPECTING ACTIVITIES OF SHEVACK

I. Background

71. Shevack has been engaged in the offer and sale of investment interests or participations since his affiliation as a Distributor in Koscot. (See F.F. 8 and 9, supra).

72. Shevack was known to the Galaxy management by virtue of his expertise in various prospecting methods including one known as "cold canvassing" whereby total strangers were accosted on the street and invited to attend recruitment meetings. Shevack employed primarily two approaches when he initially met a prospect. The first was the "curiosity approach" whereby Shevack aroused the prospect with the potential of huge financial gains in Galaxy. The second approach was the "friendly approach" whereby Shevack would induce prospects to attend Galaxy meetings by personally chauffeuring them to and from meetings. (See F.F. 8 and 9, supra, T. 341-342, 343-349, 355 1515-1517)

J. Prospecting and Closing of Branch Simmons

73. Branch Simmons ("Simmons") was approached by Shevack, a stranger to him, while waiting at a traffic light. Shevack invited him to an Opportunity Meeting, where Shevack said he would explain how to make a lot of money. The name Galaxy was not mentioned. (T. 1109-1110)

74. Simmons attended three or four Opportunity Meetings and one Sunday Step-Up meeting before joining Galaxy; Shevack was present at each meeting and was observed by Simmons to applaud when $60,000 was written on the blackboard at each meeting. (T. 1112, 1114, 1120)

75. Shevack sat next to Simmons during the first Opportunity Meeting attended by Simmons. Following the formal speeches, Shevack made the following statements to Simmons to persuade him to invest in Galaxy:

(a) that Simmons could earn $60,000 or more by investing in Galaxy;

(b) that Galaxy would obtain customers for the retail sale of food by means of radio and newspaper advertisements;

(c) that a number of customers so obtained would be assigned to Simmons to service;

(d) that Simmons would earn commissions on the sale of food to these customers;

(e) that Simmons could also earn commissions by introducing people to invest in Galaxy;

(f) that Simmons' only role in earning money on sale of franchises was to get people to come to Opportunity Meetings where Shevack would get them to invest;

(g) that any investment made by Simmons would be a guaranteed investment in that Galaxy would buy back his franchise if Simmons was not totally satisfied for any reason.

(T. 1116-1119, 1122-1123, 1140, 1159)

76. At other Opportunity Meetings attended by Simmons, in or about June, 1972, Shevack represented that retail food operations would begin by approximately July, 1972, and thereafter on subsequent dates; whereas food deliveries did not begin on those dates. Shevack also represented that food delivery operations would be made in

Brooklyn, Manhattan, upstate New York and Long Island, whereas deliveries were made in a small area around 303 Stanley Avenue, Brooklyn, the warehouse. Shevack also represented that he had earned enough money in Galaxy to buy a Cadillac Eldorado. (T. 1121, 1122, 1133, 1167)

77. During his discussions with Simmons at or following Opportunity Meetings or during Simmon's association with Galaxy, Shevack omitted to inform him of the following essential facts:

(a) that Galaxy would not be able to begin food operations unless it continued to get people to invest in Galaxy;

(b) that Galaxy would not be able to continue food operations, once begun, without continued new investments in Galaxy;

(c) that new investors were required to attend training sessions before becoming eligible to earn commissions;

(d) that new investors were required to purchase business cards, identification cards and business manuals after investing in Galaxy;

(e) that Lee, Kirsch and other management officers would receive commissions for every person Simmons or any other investor brought into Galaxy;

(f) that Shevack did not earn $60,000 a year in Galaxy;

(g) that no investor earned $60,000 in a single year in Galaxy.

(T. 1130, 1133, 1135, 1148, 1150-1151, Def.'s Exh. G)

78. Simmons informed Shevack of his lack of funds for a Galaxy investment and Shevack advised Simmons to take out a loan. Shevack subsequently drove Simmons in Shevack's Cadillac Eldorado to a branch office of the Bank of North America, where Shevack then obtained and filled out a loan application for Simmons, listing furniture rather than Galaxy investment as purpose for the loan. Simmons then signed the application and returned it to the bank manager. (T. 1141-1146, 1167)

79. When Simmons learned that his application had been approved for the loan, Shevack again chauffeured Simmons to the bank to pick up the loan proceeds. Simmons signed over his loan proceeds check for $2,009 to Shevack who told Simmons he was taking the check to give to Galaxy. (T. 1144-1146)

80. While filling out the loan application for Simmons, Shevack represented that Simmons would be able to make his investment ($2000) back in two or three weeks. (T. 1143)

81. Simmons repeatedly requested from Shevack his Galaxy application and agreement form and his $9 change from the bank check of $2,009. Shevack had promised Simmons his application and $9 change but Simmons never received either from Shevack. (T. 1141-1146, 1167)

82. When Simmons brought prospects to Galaxy meetings he introduced them to Shevack, as he had been instructed to do, F.F. 75(f), supra, and relied upon Shevack to "close" the prospects and convince them to invest in Galaxy. The

$1000 received by Simmons as commissions was the result of Shevack inducing two prospects to join Galaxy who were recruited by Simmons. Shevack, as the sponsoring Distributor of Simmons, also received commissions on the two prospects. The extent to which Simmons relied on Shevack is evidenced by the fact that Simmons attended only a single Sunday Step-Up Meeting with one prospect, but even on that occasion Shevack did all of the talking. (T. 1174-1175)

83. Simmons did not earn $60,000 a year while in Galaxy; he received only $1,000 between joining and approximately March, 1973. Furthermore, Simmons quit the Galaxy organization in March, 1973, when he realized that Galaxy would not fulfill its promises to make food deliveries. (T. 1145-1146, 1147, 1151)

K. Prospecting and Closing of Melvin McLean

83. In the summer of 1972, Melvin McLean ("McLean") was approached on the street by Shevack, a stranger to him, in a late model car, and was asked, "How would you like to

earn about $50,000 a year." McLean was given an invitation card, and invited to attend an Opportunity Meeting where Shevack represented he would show McLean how to make about $50,000 a year. In response to a question of how do you make such money, Shevack refused to give details. (Pl.'s Exh. 32, T. 1208, 1211)

84. Shevack was present and sitting next to McLean at the first Opportunity Meeting McLean attended. McLean observed Shevack cheer and applaud when people announced they were joining Galaxy and when the figures $48,000 - $60,000 were written on the blackboard. (T.1212, 1218)

85. Following the formal speeches, Shevack conversed with McLean about his job, where he lived and offered to chauffeur McLean home in Shevack's late model Cadillac Eldorado. During the ride, Shevack said he was making less than McLean while working on Wall Street before joining Galaxy, but had been able to make $30,000 - $40,000 in Galaxy, enough money to purchase the Cadillac and was purchasing a house. (T. 1212, 1218-1219)

86. Shevack asked McLean to join Galaxy, but McLean responded he did not have the money. Shevack then stated to McLean "If you really want to join Galaxy I can get you into Galaxy." Shevack then discussed with McLean his current financial status and employment. (T. 1218)

87. Shevack then drove McLean home, and Shevack explained to McLean his "rags to riches" story and how his "good friend, Artie Lee" told him about Galaxy. Shevack told McLean that he had to borrow the money to join Galaxy and then stated "you know I can help you get the money to join." (T. 1219)

88. A few days subsequent to the Opportunity Meeting McLean attended, Shevack telephoned him and suggested McLean take out a bank loan to join Galaxy. McLean offered resistence to this idea and told Shevack that he already had outstanding loans, but Shevack hammered the point to McLean that its for "your family" and "you won't regret it." (T. 1221, 1264)

89. Shevack called McLean the next day and arranged to ake him to the Bank of North America. (T. 1222)

90. Shevack met McLean and accompanied him into the bank. Shevack instructed McLean to state on the loan application that the loan proceeds were to be used for furniture and not to invest in Galaxy. Shevack also instructed McLean to claim on the application that his wife was currently working for a company in Brooklyn. To McLean's protestations, Shevack stated that the false assertion of employment would be verified by people in the company if the bank called. Shevack told McLean "I have obtained loans for most of the people I brought in this way." McLean submitted the loan application to the bank. Several days later Shevack called McLean to tell him the loan had not been approved. (T. 1221-1222, 1225-1226)

91. Shevack subsequently chauffeured McLean to a Household Finance Company office which was selected by Shevack as the source to get McLean the money to invest in Galaxy. (T. 1226-1227, 1229)

92. Shevack again instructed McLean to state on the loan application that the purpose of the loan was to purchase furniture, and in addition

to ask for only $1,000 because of the "better chance of obtaining the loan". McLean followed Shevack's instructions. (T. 1229-1230)

93. McLean's loan application was approved by Household Finance but only for the sum of $700. Shevack again chauffeured McLean, this time to pick up the loan proceeds. Shevack took the check from McLean, stated that it would be deposited with Galaxy, said "Congratulations", and had McLean sign a Galaxy contract. (T. 1230-1232)

94. To finance the difference between the loan proceeds from Household Finance Co. and the $2,000 necessary to purchase a Manager investment, Shevack invited McLean, during a Sunday Step-Up Meeting, to get three people willing to join Galaxy, which would earn McLean a fee of $500 per person. McLean subsequently sponsored three individuals into Galaxy; after each joined Galaxy Shevack affirmed to McLean that $500 had been paid into Galaxy on McLean's behalf. (Pl.'s Exh. 33, Def.'s Exh. G, T. 1233, 1238-1242)

95. McLean then asked Shevack for a copy of his contract with Galaxy and his badge to show he was a Manager. Shevack kept stalling McLean on the production of his contract and told him "Don't worry, everything is O.K." (T. 1242-1244)

96. McLean then complained to the Galaxy management that Shevack had not given him his Manager contract and all the events described in F.F. 94 to 95, supra. As a result of several Galaxy executives speaking to Shevack in private, McLean was issued an approved Manager contract on or about October 8, 1972. (Pl.'s Exh. 33, T. 1244-1250)

97. The loan money Shevack received from McLean and the commission owing to McLean from his sponsoring three individuals into Galaxy had not been paid or deposited into Galaxy as Shevack had represented to McLean. (Def.'s Exh. G, T. 404-405)

98. As in the case of Simmons, McLean relied on Shevack to sponsor and induce his prospective investors to join Galaxy. Shevack's instructions

to McLean were simply to get them (potential investors) to the meetings to meet Shevack, and he (Shevack) would handle the rest. Shevack would then take over, he would even go to their homes (without McLean), discuss the Galaxy operation and arrange for the financing so they could join. (T. 1240, 1285-1287, 1292)

99. Shevack represented to McLean that he (McLean) had a "guaranteed investment" in Galaxy. McLean was specifically told by Shevack that if after McLean had been associated with Galaxy for six months or one year, and if Galaxy was not funtioning to McLean's expectations, then he could get his investment back in full, less commissions paid by Galaxy. (Pl.'s Exh. 34; T. 1259)

L. Prospecting and Closing of Mr. and Mrs. Silverman

100. After hearing of Galaxy through a friend of Mrs. Silverman's, Mr. and Mrs. Silverman were contacted by telephone by Shevack, a stranger to them, and were invited to an Opportunity Meeting of Galaxy. Shevack said in that

conversation that a lot of money could be made in Galaxy but refused to answer questions about details, saying the meeting would explain what Galaxy was about. Shevack picked the Silvermans up and chauffeured them to a Galaxy Opportunity Meeting in his Cadillac Eldorado. During the drive, Shevack again told the Silvermans that there was a lot of money to be made in Galaxy, that he had made a lot of money already and bought the Cadillac from his earnings. Shevack again declined to give details about Galaxy. (T. 1305-1307, 1401-1402)

101. After attending this first Opportunity Meeting, Shevack chauffeured the Silvermans to their home, during which trip Mr. Silverman conveyed their interest in Galaxy, but said he did not have the money to invest, and Mrs. Silverman was unemployed. Shevack said this was not a problem, as he would assist them to get small loans from different finance companies and banks. Shevack instructed the Silvermans:

(a) to list furniture as the purpose of the loans rather than an investment in Galaxy;

(b) that he (Shevack) would supply a phoney W-2 form to show Mrs. Silverman was employed;

(c) not to disclose to each bank or finance company that multiple simultaneous loan applications were being made with other banks and finance companies.

(T. 1319-1322, 1343-1349, 1403-1404, 1408, 1411-1412)

102. In response to Mr. Silverman's uneasiness about these methods for obtaining loans, Shevack represented to the Silvermans that he had used the above methods of obtaining loans before and that the methods worked. Shevack also stated that the price of a Galaxy franchise would rise, and that loans were the only way to get the money. (T. 1323-1325, 1349, 1408)

103. Shevack chauffeured the Silvermans to six different banks and finance companies in Manhattan and Brooklyn, five the first day and one on a subsequent day, for the purpose of applying for loans to invest in Galaxy. In the course of the first day, Shevack gave the Silvermans a

W-2 form, which listed Mrs. Silverman as being employed by A & M Dental Labs, a company unknown to the Silvermans at that time; Shevack also gave the Silvermans a slip of paper on which the Silvermans observed Shevack to write the name, address, and telephone number of A & M Dental Labs, to which paper Mrs. Silverman added the name, "Francis Alexander" and "$165.00", at Shevack's direction. Shevack assured the Silvermans that he had contacts at A & M Dental Labs who would confirm the false claim that Mrs. Silverman was employed. (Pl.'s Exhs. 36, 37, t. 1320-1325, 1403-1407)

104. At the first five lending institutions to which Shevack chauffeured them, Mr. and Mrs. Silverman filled in loan applications in accordance with Shevack's instructions: listing furniture as the purpose of the loan, using the W-2 form and information supplied by Shevack to substantiate Mrs. Silverman's ostensible employment, and omitting the fact that other loan applications were made or would be made simultaneously. Shevack imposed a different procedure which was followed for the sixth institution, Family Finance Co. After

the proceeds of loans from the first five institutions was found to be insufficient to purchase the Galaxy investment, Shevack informed the Silvermans that he had called Family Finance Co. and given the necessary information over the telephone including the fact that Mr. Silverman had received a loan from Household Finance Co. The Silvermans signed an application that had already been filled in, listing furniture as the reason for the loan and Mrs. Silverman's ostensible employment. (Pl.'s Exhs. 38, 39, 40; T. 1321, 1325-1328, 1345, 1376, 1407-1413)

105. The Silvermans received approximately $6,300 in loan proceeds from four financial institutions, which was supplemented by approximately $400 from a savings account, and approximately $300 borrowed from Shevack, and was used to purchase a Galaxy distributor investment costing $7,000. The Silvermans signed over the checks to Shevack, to be given into Galaxy. The Silvermans did not make any money in Galaxy. (Pl.'s Exh. 35, T. 1348-1350, 1410-1411, 1432)

106. In or about November, 1972, Mr. Silverman was informed by Galaxy that he would not be able to earn commissions for the retail program as he had been informed at the time he joined Galaxy. (T. 1318-1319, 1447-1448, 1456-1457, 1460)

107. In December, 1972 Mr. Silverman requested in writing the return of his investment. His request was never acknowledged by Galaxy and his investment was not refunded. (Def.'s Exh. R, 1350)

M. Financial Gain from Galaxy

108. Between approximately June, 1972 and approximately July, 1972, Shevack sponsored individuals into Galaxy and as a result of these individuals' purchases of investment interests, received $5,000 pursuant to a private agreement with Lee which $5,000 was used by Shevack to purchase a Galaxy distributorship in approximately mid-July, 1972. (T. 1473-1476, 1556)

109. Following the purchase of his Galaxy distributorship in approximately July, 1972, until he sold his distributorship in approximately December, 1972 for which he received $6,000 less $500 transfer fee payable to Galaxy, Shevack received approximately $14,000 in commissions for sponsoring 10 investors into Galaxy. (Pl.'s Exh. 42 to 42H, Def.'s Exh. G, T. 1480-1481, 1485-1486)

VI. PROSPECTING ACTIVITIES OF KIRSCH

110. Kirsch, as an officer of Galaxy and a Distributor in Koscot, was quite familiar with the various methods and techniques of prospecting. (T. 63-65)

111. Kirsch directly sponsored three individuals into Galaxy during 1971: Robert Coady ("Coady"), Morris Richter ("Richter"), and Howard Beck ("Beck"). Kirsch received the commissions as the sponsoring Distributor. Kirsch persuaded Coady and Richter to invest in Galaxy after he personally spoke to them on the Galaxy concept. (T. 45, 56-58)

N. Prospecting and Closing of Beck

112. In or about August, 1971, Beck and his brother were driving through the Queens Midtown Tunnel in New York when a second car, attracted their attention by honking its horn. Beck saw Kirsch driving the second car, both vehicles slowed down and Kirsch passed a flyer to Beck's brother. (T. 381-383)

113. The flyer spoke of earning fantastic sums of money such as "$2,000 per month," being "able to vacation two months out of every year", and being associated with a "35 year old multi-millionaire". Kirsch's name and telephone number were on the flyer. (Pl.'s Exh. 26; T. 888)

114. Thereafter Beck telephoned Kirsch concerning the flyer and Kirsch invited Beck to attend a Galaxy presentation meeting at the Summit Hotel in August, 1971. (T. 891-892)

115. Beck attended this Galaxy meeting and met Kirsch there. After the meeting, Kirsch reiterated to Beck what the speakers had already told him

about Galaxy including the figures presented during the blackboard demonstration that it was possible to earn $60,000 per year with Galaxy. (T. 395-398)

116. Beck attended one other Galaxy meeting, and a short time thereafter, Kirsch telephoned him to ask if he would invest in Galaxy. Kirsch was told by Beck that he wished to join Galaxy as a Manager for $1,000. When Beck met with Kirsch to sign the Galaxy contract, Kirsch had already filled in the contract which stated that Beck was joining Galaxy as a "Distributor for $3,000." (Pl.'s Exh. 27; T. 900-901)

117. Kirsch tried unsuccessfully to convince Beck to join as a Distributor by telling him he could earn more money in Galaxy. Beck replied that he did not have the extra $2,000. Kirsch then suggested to Beck to go to a bank with him and borrow the $2,000. (T. 903)

118. Beck told Kirsch that trying to obtain a loan was not a good idea because he had just been discharged from the Army and had no

credit references. Kirsch told Beck to use his company, K Enterprises, a company in which Beck was never employed, for a credit reference, which company was Kirsch's Distributor's trade name in Roscot. (T. 197, 904)

119. Kirsch chauffeured Beck to a Manufacturers Hanover Bank Office to fill out a loan application. Prior to going into the bank, Kirsch instructed Beck to tell the bank that the purpose of the loan was to buy furniture and not the true purpose which was to invest in Galaxy. (T. 907)

120. Beck and Kirsch went into the bank together where Beck verbally applied for the loan including telling the bank officer that the loan was for furniture. Beck did not receive the loan. (T. 907)

121. Kirsch suggested that Beck try another bank, but he refused. Beck then joined Galaxy as a Manager for $1,000 in October, 1971. (Pl.'s Exh. 27, T. 904, 909)

122. Kirsch, after inducing Coady, Richter and Beck to invest in Galaxy, began instructing these individuals on techniques of prospecting and closing of potential investors. Kirsch endorsed the use of "cold canvassing" as well as the making of representations to prospects that investing in Galaxy could earn them a large amount of money. Furthermore, Kirsch instructed these three individuals to employ the "curiosity approach" in approaching prospects, that is, not to say anything in detail about Galaxy. (T. 63-65)

123. Beck immediately began to work with Kirsch and utilized his prospecting techniques as described in F.F. 122, supra. Kirsch took Beck around to different areas to pass out flyers about Galaxy. Kirsch would stop to talk to prospects anywhere and everywhere while driving on the highway or even in restaurants. In fact, Kirsch told Beck for the first time that the flyers Kirsch had used in prospecting did not apply to Galaxy, but to another business. No attempt was made to restrict the prospecting to New York State residents. (Pl.'s Exh. 26, T. 909-910, 940)

124. Kirsch actively participated in many impromptu Galaxy training sessions for new investors during the fall of 1971 by offering suggestions to new investors on prospecting. In fact, because of Kirsch's background in Koscot, Kirsch did not have to attend training sessions as a trainee. (T. 61, 977)

125. Kirsch, at almost every Opportunity Meeting he attended prior to October, 1972, directly implemented the Executive Board policy of having board members circulate among potential investors and assist new inexperienced Managers and Distributors to close sales of investments. In fact, prospects were brought to Kirsch's office for the specific purpose of assisting in their closing, i.e., he would explain the Galaxy concept. (T. 834-835)

VII. Credibility of Kirsch and Shevack

126. Kirsch's testimony concerning his involvement in securing bank loans by means of false information and his responsibility for the sale of Galaxy investments by means of misrepresentations

and omissions of material facts has been contradicted not only by himself, but also by prior inconsistent statements, the testimony of an investor witness he recruited in Galaxy, Beck, and the President of Galaxy, Lee. (See Pl.'s Memorandum of Law in Support of Findings of Fact and Conclusions of Law, S.E.C. v. Galaxy Foods, Inc., 73 Civil 1742.

127. Shevack's testimony concerning his involvement in securing bank loans by means of false information and his responsibility for the sale of Galaxy investmetns by means of misrepresentations and omissions of material facts has been contradicted by the testimony of investor witnesses he recruited into Galaxy, namely, Simmons, McLean and Mr. and Mrs. Silverman. (See Pl.'s Memorandum of Law in Support of Findings of Fact and Conclusions of Law, S.E.C. v. Galaxy Foods, Inc., 73 Civil 1742)

VIII. Present Activities of Shevack and Kirsch

128. Futuristic Foods, Inc. ("Futuristic") was incorporated in the State of New York on

January 3, 1973. Its principal place of business is located at 62-45/57 Woodhaven Boulevard, Rego Park, New York. Futuristic was incorporated for the purported purpose of establishing a corporation which would provide a free home delivery of food and non-food supermarket items to consumers. (T. 1520, 1629-1630, Pl.'s Exh. 44)

129. The incorporators of Futuristic were Shevack, Peter Cancilla ("Cancilla"), and William Reichert ("Reichert"). The idea for the organization of Futuristic came from Shevack's prior knowledge of and association with Galaxy and Koscot. In fact, Futuristic was incorporated approximately one month after Shevack left Galaxy in December, 1972. (T. 1129-1130)

130. Specifically, Futuristic was patterned after Galaxy in the following areas:

(a) a management team and core of trained sales agents skilled in sale of franchise investments;

(b) meetings designed to give a preview of the business to potential investors

to persuade them to invest in Futuristic;

(c) mandatory training sessions for new investors; and

(d) facets of the commission structure, including commissions paid to investors sponsoring new investors into Futuristic and commissions paid to sponsors on retail sales obtained by those having the lower-priced investment.

(T. 172-174, Pl.'s Exh. 44)

131. Kirsch joined Futuristic in January, 1973 as a Vice-President in charge of Administration in Futuristic. (T. 146)

132. Shevack is presently the President of Futuristic. He has also served as Vice-President and Secretary of Futuristic. (T. 1520, 1628)

133. In order to raise sufficient capital to implement the food program, Futuristic, as did Galaxy, commenced its operations by offering

for sale and selling two types of investments to the public which are called "silver" and "gold" investments. The "silver" investment offered and sold initially cost $2,000 but now sells for $3,000. The "gold" investment initially sold for $5,000, but now sells for $6,000. (Pl.'s Exh. 44, T. 148-149, 176, 1632)

134. The "gold" or "silver" investment holder basically receives the following: business training; sales training for himself and his salesmen; the right to use the charge plan when initiated; free delivery service to his customers; and commissions commensurate with his investment interest on initial retail orders and re-orders. However, before August 23, 1974, commissions and incentive bonuses were also paid to investment holders who sponsored new investors into Futuristic. (Pl.'s Exh. 44, T. 1520-1521)

135. Kirsch and Shevack are presently Vice-President and President of Futuristic, respectively, and continue to draw salaries in those positions. (Pl.'s Exh. 44 and updated edition, T. 146, 1520, 1642)

PLAINTIFF'S FINDINGS OF FACT AND CONCLUSIONS OF LAW

CONCLUSIONS OF LAW

1. This Court has jurisdiction of the parties and of the subject matter of this action.

2. During the period from on or about September 2, 1971 to on or about November 28, 1973, in the Eastern District of New York and elsewhere, defendants Kirsch and Shevack wilfully violated Sections 5(a) and 5(c) of the Securities Act of 1933, 15 U.S.C. 77e(a) and 77e(c) in that directly and indirectly, singly and in concert they offered for sale, sold and delivered after sale certain interests which constitute investment contracts, certificates of interest, or participations in profit sharing agreements and interests commonly known as securities, all within the definition of "security" as set forth in Section 2(1) of the Securities Act of 1933, 15 U.S.C 78c(a)(10), while and at a time no registration statement covering such interests or securities was in effect.

3. During the period from on or about September 2, 1971 to on or about November 28, 1973, in the Eastern District of New York and elsewhere, defendants Kirsch and Shevack wilfully violated Section 17(a) of the Securities Act of 1933, 15 U.S.C. 77q(a), and Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. 78j(b) and Rule 17 C.F.R. 240.10b-5 thereunder in that, directly and indirectly, singly and in concert, in connection with

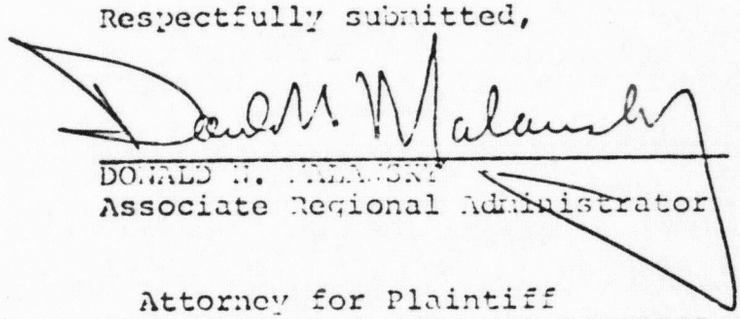
the purchase and sale of securities referred to in paragraph 2, supra, and by the use of the means and instrumentalities of transportation and communication in interstate commerce and of the mails, they employed devices, schemes and artifices to defraud; obtained money and property by making untrue statements of material facts and omitting to state material facts necessary to make the statements made, in light of the circumstances under which they were made, not misleading; and engaged in acts, practices, and courses of business which operated as a fraud and deceit upon purchasers and prospective purchasers of the securities of Galaxy referred to in paragraph 2, supra.

4. The defendants Kirsch and Shevack singly and in concert, made use of the means and instruments and instrumentalities of transportation and communication in interstate commerce and of the mails while engaged in the illegal conduct described in paragraphs 2 and 3, supra.

5. The issuance of a permanent injunction is essential to protect the public against a repetition of the violations described in paragraphs 2 and 3, supra. Unless the defendants Kirsch and Shevack are enjoined, there is a strong likelihood that they will continue to engage in violations of the federal securities laws with respect to the securities described in paragraph 2 supra, or any other securities.

6. To insure the full impact of the deterrent force of the securities acts and to insure adequate enforcement of the securities acts, Kirsch and Shevack should be required to disgorge all money or other consideration received by said defendants from the sale of Galaxy securities, in the form of commissions or in whatever forms those funds may now appear.

Respectfully submitted,



DONALD M. MALAMSKY
Associate Regional Administrator

Attorney for Plaintiff
SECURITIES AND EXCHANGE COMMISSION
New York Regional Office
26 Federal Plaza
New York, New York 10007
Telephone No.: (212) 264-1634

OF COUNSEL:

Franklin D. Ornsten
Allan M. Lerner
Harry L. Garmansky
Regina C. Mysliwiec
Julia B. Williams

Dated: New York, New York
November 29, 1974

DEFENDANTS SHEVACK AND KIRSCH'S FINDINGS OF FACT AND CONCLUSIONS OF LAW.

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

-against-

GALAXY FOODS, INC.,
ARTHUR LIEBERMAN a/k/a ARTY LEE
RALPH AVNI
CHARLES HOROWITZ
BRUCE KATZ
STEVEN ROTH
MARK GLAZER
IRWIN DONALD KIRSCHENBLATT a/k/a
DONALD KIRSCH
GEORGE PADILLA
ARTHUR SHEVACK,

73 Civil 1742

Defendants.

This cause coming on for trial and the Court acting as the trier of facts is hereby requested to make the following findings of fact and to state the conclusions of law as follows:

FINDINGS OF FACT

1. That the defendant, GALAXY FOODS, INC., is a domestic corporation organized and existing under the Laws of the State of New York.

2. That the defendant, GALAXY FOODS, INC., maintains its places of business in the City and State of New York.

3. That the defendant, GALAXY FOODS, INC., maintains no places of business outside of the State of New York.

4. That the defendant, DONALD KIRSCHENBLATT, was an employee of GALAXY FOODS, INC. (p.25,227)

5. That the defendant, DONALD KIRSCHENBLATT, was a Vice-President of the defendant, GALAXY FOODS, INC. (p.31)

6. That the defendant, DONALD KIRSCHENBLATT, was not a director of the defendant, GALAXY FOODS, INC., although it would appear that he was a member of a committee in which were various officers of the corporation as well as directors, shareholders and at times other employees. (pp.31-35)

7. That the corporation referred to the meetings at which all of the aforesaid individuals attended as "director meetings."

8. That it referred to its meetings of its Board of Directors as "Executive Board" meetings. (pp.48,49)

9. That, in essence, the meetings of the "Executive Board" were in fact meetings of its Board of Directors; and the meetings referred to as "Board of Directors" meetings were in fact meetings of its officers and employees. (pp.48,49,211-215, 458-9)

10. That the policy for the operation and management of Defendant Galaxy were decided by the owner-officers and then presented to the "Board of Directors", not for their approval, but merely to apprise them of such policies. (pp.87, 636)

11. That the "Board of Directors" could offer

suggestions to the management of the defendant Galaxy, but could not act on such suggestions until they had been approved by the management.

12. That the management of defendant Galaxy held an absolute veto over all policies and activities of the defendant corporation and its employees.

13. That the business of the defendant corporation was both the sale of franchises and the sale of food to the general public.

14. That, by the defendant Galaxy's own rules and regulations, no sale of a franchise could be made until the defendant Galaxy had approved the prospective franchisee's application.

15. That no sale or offer to sell could be made by any person save the defendant Galaxy.

16. That the actions of any person with respect to the contacting of prospective franchisees, or "cold canvassing", etc., were merely ministerial in nature, in that such actions were the execution, by such persons, of the instructions given them by the defendant Galaxy.

17. That the defendant Galaxy had begun its retail operations, in that it had rented a warehouse and trucks, and it had purchased shelving, a freezer and refrigerator unit, a computer, cathode ray tubes, floor-lifts, scales, and it had employed up to nearly 100 people to service, package, weigh, cut

and deliver food. (pp.609-613)

18. That during its pilot program, the defendant Galaxy actually sold approximately $160,000 worth of food.(p.606)

19. That the defendant Galaxy spent approximately $210,000 in acquiring food. (p.607)

20. That at the time of defendant Galaxy's demise, in August, 1973, it had procured approximately 4,800 retail customers. (p.846)

21. The defendant, DONALD KIRSCHENBLATT, was employed as a marketing specialist for the defendant corporation. (pp.127,275)

22. That the defendant, ARTHUR SHEVACK, was neither an officer, shareholder, director nor executive committee member. (p.1475)

23. That the defendant, ARTHUR SHEVACK, had, for consideration, purchased a franchise from the defendant corporation. (p.1475)

24. That the defendant, DONALD KIRSCHENBLATT, had likewise purchased a franchise from the defendant corporation the purchase of which was made by the payment to the corporation of time and services as distinguished from the payment of monies. (pp.36,201)

25. The services performed by the defendant, DONALD KIRSCHENBLATT, for andin behalf of the defendant corporation were in the nature of work required to be performed so as to

enable the defendant corporation to market food products to the general public. (pp.127,132,143,206,277,451,498)

26. That the defendant, DONALD KIRSCHENBLATT, at the commencement of his employment, did receive, as a finder's fee or commission, but one sum of $700.00 from the defendant GALAXY on account of the sale by it of one of three franchises. (pp.47,201)

27. That the defendant, ARTHUR SHEVACK, did receive, as finder's fees or commissions, monies from the defendant GALAXY on account of the sale by it of between six and ten franchises, after arrangements had been made for the purchase by the defendant SHEVACK of his own franchise.

28. That the testimony reveals that both defendants ARTHUR SHEVACK and DONALD KIRSCHENBLATT understood that the defendant corporation was going to market food and eatable products to the general public in addition to the sale by it of franchises.

29. That the evidence reveals that from the date of his employment to the date of the termination of his employment the defendant, DONALD KIRSCHENBLATT, devoted virtually all of his time and effort as an employee of said corporation to the preparation of a catalog required for the customers who were to purchase food from the corporation by the use of such catalog and in surveying the wholesale food

industry with a view toward the actual purchasing of food by the corporation for ultimate retailing of same to the general public. (p.497-8)

30. That at no time did the corporation request the consent of either the defendant KIRSCHENBLATT or the defendant SHEVACK for its failure to market food to the general public or for its failure to make payment of commissions on account of the solicitation for the sale or the actual sale of such food.

31. That notwithstanding that the executive committee (the actaul Board of Directors) appears to have modified, unilaterally, the terms of the written agreement between it and its franchisees, as relates to the sale of food and the payment of commissions, neither the defendant SHEVACK nor the defendant KIRSCHENBLATT were asked to consent to the policy of the management to limit or postpone the payment of commissions until the corporation first procured 8,000 to 10,000 customers. (pp.39,133)

32. That the restriction on the payment of commissions to a date after the procurement of the first 8,000 retail customers was neither set forth in the contract between the corporation and its employees, nor acquiesced in by the franchisees, nor predicated upon any vote taken at any meeting whereat the said franchisees were given the opportunity to voice their opinion or to cast vote in connection with said

modification of their various agreements of franchise. (pp.39,133)

33. That the defendant, ARTHUR SHEVACK solicited retail business for the sale of food to the general public from approximately 200 individuals, of which approximately 50 did receive shipments of food. (pp. 1482,1547)

34. That the contractual obligation between the defendant corporation and the defendant, ARTHUR SHEVACK, called for the payment to the defendant, ARTHUR SHEVACK, of commission on the sale of said food.

35. That the defendant corporation at no time paid to the defendant, ARTHUR SHEVACK, commission on the sale of any food to any of the customers whose business had been solicited by the defendant, ARTHUR SHEVACK. (p.514)

36. That the record reveals that the defendant KIRSCHENBLATT did not participate in any meetings of the corporation, save to the extent that he would report at said meetings the work undertaken by him and the progress made by him in connection with the retailing of food, contacts made by him with various suppliers of food and information obtained by him which would be utilized in connection with the preparation of a catalog needed for the marketing of said food and the ultimate distribution of said food; and in addition, he did communicate at training sessions, methods and procedures to be utilized by the franchisees with regard to the actual sale and marketing of products at retail; and, in addition, he did on a single occasion, speak at one opportunity meeting. (pp. 49, 60, 203, 205, 309, 428-430, 523)

37. That the defendant Kirschenblatt was unaware of any premeditated plan to cheer and applaud at specific times during the Opportunity and Step Up meetings. (p.66-67)

38. That the record will reveal that the defendant, ARTHUR SHEVACK, at no time spoke at any meetings of the corporation, including but not limited to, executive board meetings, Board of Director meetings, opportunity meetings, step-up meetings or training sessions. (pp. 309, 337,1497-1498)

39. The record will reveal that the defendant, ARTHUR SHEVACK, did speak at one meeting of franchisees which meeting was not sponsored or held pursuant to the direction of the corporation, but rather was convened at the request of a limited number of franchisees.

40. That the management of defendant Galaxy set a ceiling limit of 1079 distributorships that could be sold, of which approximately 803 were sold. (pp.553,586-587)

41. That the defendants ARTHUR SHEVACK and DONALD KIRSCHENBLATT were but two of said franchisees.

42. That neither the defendant, ARTHUR SHEVACK, nor the defendant, DONALD KIRSCHENBLATT, were rated amongst the top franchise salesmen of the defendant corporation; and indeed the record will disclose that neither was amongst the top 10 franchise salesmen performing services of that nature for and in behalf of the defendant corporation. (pp.565-566)

43. The record will further reveal that all of the named defendants but one such defendant, to wit, GEORGE PADILLA

was amongst the top 10 franchise salesmen.

44. That with one exception, the only remuneration paid to the defendant Kirschenblatt was a percentage of the gross sales, which was paid to him biweekly, not at a Sunday Step-Up meeting, and was considered in the nature of a salary. (pp.44, 282-286,292-293)

45. That the defendant Kirschenblatt prepared only the "Supermarket Analysis" portion of the Galaxy Distributors Guide. (Plaintiff's exhibit 11 for identification) (pp.389-390)

46. That defendant Kirschenblatt was not called upon to approve the other portions of the Guide but others were called upon to pass upon, or approve, what the defendant Kirschenblatt had prepared. (p.39)

47. That the only documents prepared by the defendant Kirschenblatt were those relating to the retail sale of food, namely the marketing catalog, the price lists, and the Supermarket Analysis portion of the Distributors Guide.

48. That the defendant Shevack never prepared any documents, brochures or ads for publication.

49. That the defendant Kirschenblatt first became aware of the newspaper ads when it was shown to the "Board of Directors" by defendant Arthur Lee and the other owners who informed the Board that the ad was going to be published in the newspapers. (p.72)

50. That the management of defendant Galaxy, the owner-officers, were the sole authors of the Opportunity meeting scripts; defendant Kirschenblatt had nothing to do with the preparation thereof. (pp.370-371)

51. That the only persons given the privilege of operating an automobile owned by the defendant corporation were the owner-officers. (p.497)

52. That the defendant DONALD KIRSCHENBLATT, terminated his employment with the defendant corporation in January, 1973.

53. That the defendant Kirschenblatt terminated his employment with defendant Galaxy when he finally realized that it would be impossible for defendant Galaxy to carry out its plans for full scale retailing of food. (pp.224-226)

54. That the defendant, ARTHUR SHEVACK, terminated his association with the defendant corporation in or about December, 1972. (p.1480)

55. That the termination of the relationship between the defendant, ARTHUR SHEVACK, and the defendant corporation was brought about at the time of the sale by said individual defendant of his franchise which had been previously purchased by him from the defendant corporation. (pp.511,1481)

56. That there is no testimony before the Court to reveal that either the defendant, ARTHUR SHEVACK, or the defendant, DONALD KIRSCHENBLATT, participated in the sale of any

franchises through the utilization of the United States mails or by use of the telephone; and although there is some testimony to the effect that someone called ARTHUR SHEVACK to arrange an appointment between him and two prospective franchisees for the purpose of arranging for ARTHUR SHEVACK to drive them to an Opportunity meeting, there was no solicitation made by him at that time.

57. The testimony will reveal, however, that the defendant corporation did, at times, avail itself of the use of the telephone and the use of the United States mails in connection with the solicitation for the sale of franchises to the general public.

58. There is no testimony to reveal that the conduct of the defendant corporation in contacting prospective franchises by use of the telephone and the mails, was ever communicated to either DONALD KIRSCHENBLATT or ARTHUR SHEVACK; to the contrary, there is testimony throughout the transcript indicating that all franchisees were specifically advised to refrain from the utilization of such means of communication and to limit their activities to face-to-face meetings with prospective franchisees and, even then, to limit any discussion had between them and prospective franchisees to the extent of convincing them to attend an opportunity meeting.

59. The testimony will reveal that a franchisee could not consumate a sale of a franchise to another; rather,

a franchisee could do nothing more than refer a prospective franchisee to the corporation.

60. A franchisee could not bind the corporation by contract or otherwise.

61. The individual franchisee could act as nothing more than a finder and receive, in the event of the sale of a franchise to another, a finder's fee.

62. The conduct of a franchisee in relation to the solicitation of additional franchisees was nothing more than the performance of a ministerial act.

63. There is nothing contained in the record which would indicate that any improper conduct of the corporation could be imputed to the individual defendants KIRSCHENBLATT and SHEVACK.

64. There is nothing in the record to indicate that either SHEVACK or KIRSCHENBLATT ever uttered any statement containing false and misleading facts as relates to the nature of the operation of the defendant corporation.

65. There is nothing contained in the record to indicate that SHEVACK or KIRSCHENBLATT ever induced anyone to purchase a franchise or attend an opportunity meeting through misstatement of fact.

66. There is nothing to indicate that any of the individuals referred to an opportunity meeting by SHEVACK or KIRSCHENBLATT misunderstood the nature of the business or

were other than fully cognizant of the nature of the corporation's business, the nature of the work that would have to be performed, or the nature of the remuneration they would hope to receive; to the contrary, each of the witnesses placed on the stand by the plaintiff acknowledged the fact that they were cognizant and fully aware of the nature of the defendant corporation's business.

67. There is nothing in the record to indicate that either KIRSCHENBLATT or SHEVACK endeavored to mislead, confuse or otherwise misrepresent.

68. While there is testimony to the effect that the defendant SHEVACK induced individuals to prepare improper financial statements so as to obtain bank loans, such conduct, even if engaged in, in no way indicates an attempt to misrepresent any of the facts relevent to the nature of the defendant's business or the conduct that would be expected of the prospective franchisee, should he purchase a franchise; and as relates to the question of SHEVACK endeavoring to induce individuals to prepare false financial statements, the record, even then, leaves suspect the motive of the witnesses, and the fact as to whether SHEVACK did endeavor to pursuade them to obtain loans in that manner. In this regard, at least two of the witnesses who claim that SHEVACk prepared a false W2 form so as to enable them to obtain a loan is belied by the fact

that the alleged W2 form contained information which only the individuals themselves knew and which admittedly had never been communicated to SHEVACK.

69. The facts reveal that while at best a fraud may have been committed upon a bank or banks, no fraud was ever committed upon any of the prospective franchisees including those contacted by the defendants KIRSCHENBLATT and SHEVACK.

70. The record is devoid of any evidence that would indicate that SHEVACK or KIRSCHENBLATT intended to deceive any prospective franchisee or investor.

71. The record is devoid of any evidence to indicate that either SHEVACK or KIRSCHENBLATT knowingly communicated any misst-tement of fact and there is consequently an absence of scienter which must necessarily be demonstrated to have existed before one may be held accountable for fraud.

72. To establish the commission of a fraud upon any individual, it is incumbent upon plaintiff to demonstrate reliance by the individual allegedly damaged upon a material misstatement of fact; the record is devoid of any evidence indicating reliance by anyone upon a misstatement of material fact.

73. The record is devoid of any evidence indicating that any monies received by the corporation on account of the purchases of franchises were used to capitalize the defendant corporation; and while the plaintiff would wish the Court to infer such a fact, in order to confer jurisdiction upon it, there is no basis upon which the Court can properly make such an

inference; indeed, the plaintiff has failed completely to demonstrate the manner in which the defendant corporation was capitalized; failed to submit the corporate books; failed to investigate into the Charter and By laws; failed to put on any witness, expert or otherwise to testify as to the nature and manner of capitalization and failed to offer into evidence any of the tax returns of the corporation which might bear upon the question of capitalization.

74. The record reveals that each of the individual franchisees had to perform considerable services in their own behalf in order to realize any gain from either the sale of franchises or the sale of food at retail.

CONCLUSIONS OF LAW

1. The weight of the credible evidence prevents a finding of a commission of a fraud by either KIRSCHENBLATT or SHEVACK as relates to any prospective or actual investor of Galaxy Foods Inc.

2. No act of the defendant corporation may be imputed to either the defendant KIRSCHENBLATT or SHEVACK unless it is first demonstrated that they conspired to commit said act or knowingly aided and abeted the commission of said act.

3. Having failed to demonstrate that funds procured by the defendant corporation from franchisees were utilized to capitalize the defendant corporation, this Court

lacks jurisdiction of the subject matter.

4. The record having revealed that the franchisees of the defendant corporation were required to expend time, effort and money (other than by way of the initial purchase price of a franchise) precludes this Court from maintaining jurisdiction over the subject matter in light of Security and Exchange Commission v Howey 328 U.S. 293 (1946).

5. Plaintiff has failed to prove a cause of action either in fraud or as may relate to the alleged sale of a "security".

Accordingly, plaintiff's complaint and each and every cause thereof, is dismissed with prejudice.

EDWARD R. NEAHER
Judge of the United States
District Court,
Southern District of New York

Respectfully Submitted,

GOIDEL, GOIDEL & HELFENSTEIN

By: Alvin I. Goidel,
Member of the Firm
Attorneys for Defendants SHEVACK and KIRSCHENBLATT
Office & P.O. Address:
127 John St.
New York, N.Y. 10038
Tel. (212) 952-0370

MEMORANDUM DECISION PERMANENTLY ENJOINING DEFENDANTS.

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

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SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

-against-

GALAXY FOODS, INC., ARTHUR LIEBERMAN a/k/a ARTY LEE, RALPH AVNI, CHARLES HOROWITZ, BRUCE KATZ, STEVEN ROTH, MARK GLAZER, IRWIN DONALD KIRSCHENBLATT a/k/a DONALD KIRSCH, GEORGE PADILLA, ARTHUR SHEVACK,

Defendants.

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MEMORANDUM OF DECISION

APPEARANCES:

WILLIAM D. MORAN, ESQ.
Attorney for Plaintiff
Securities and Exchange Commission
By FRANKLIN D. ORMSTEN, ALLAN M. LERNER, HARRY L. GARMANSKY, REGINA C. MYSLIWIEC, JULIA B. WILLIAMS, ESQS., Of Counsel

GOIDEL, GOIDEL & HELFENSTEIN, ESQS.
Attorneys for Defendants
Kirschenblatt & Shevack
By ALVIN I. GOIDEL, ESQ.

NEAHER, District Judge.

Plaintiff Securities and Exchange Commission ("SEC") brought this action pursuant to §20(b) of the Securities Act

of 1933 ("the Securities Act"), 15 U.S.C. 77t(b), and §21(e) of the Securities and Exchange Act ("the Exchange Act"), 15 U.S.C. 78u(e), alleging violations by defendants of the §5 registration provisions of the Securities Act, 15 U.S.C. 77(e), and the anti-fraud provisions of both acts, §17(a) of the Securities Act and §10(b) of the Exchange Act, 15 U.S.C. 77q(a) and 15 U.S.C. 78j(b). Named as defendants are Galaxy Foods, Inc. ("Galaxy") and Arthur Lieberman, Ralph Avni, Charles Horowitz, Bruce Katz, Steven Roth, Mark Glazer, Irwin D. Kirschenblatt, George Padilla and Arthur Shevack, all of whom were either directors, officers or franchisees of Galaxy. The relief sought includes, inter alia, a permanent injunction against future violations of the securities laws and disgorgement of profits.[1]

Prior to the hearing on the merits, defendants Lieberman, Avni, Horowitz, Katz, Roth and Glazer consented to the entry against them of a judgment, which included a broad permanent injunction against future violations of the securities laws and a provision for disgorgement of specified dollar amounts, without admitting or denying any of the substantive allegations of the complaint. During the hearing, which lasted eight days, Padilla also consented to the

entry of a similar judgment against him and the matter proceeded to conclusion solely against Kirschenblatt and Shevack.

The following constitute the court's findings of fact and conclusions of law. Rule 52(a) F.R.Civ.P.

I. Galaxy Foods, Inc.

Galaxy was incorporated on September 2, 1971 by Lieberman, Avni and Rosenthal, each of whom acquired its issued and outstanding stock in approximately equal amounts in exchange for a total capital contribution of $100. Rosenthal became chairman of the board of directors and president; Avni became vice-president and Lieberman became secretary-treasurer.[2]

In October 1971, Galaxy rented a large room on Flatbush Avenue in Brooklyn which served as its principal business office. This room was subdivided into compartments and used by Galaxy's executives as individual offices. In March 1972, Galaxy rented a warehouse on Stanley Avenue in Brooklyn.

Galaxy's proclaimed business objective was to provide a free home delivery service of supermarket items. Galaxy's retail customers would order name brand supermarket

items at competitive prices from a catalog prepared by Galaxy and Galaxy would fill those orders from inventory.

In order to make possible this new concept in food retailing, two important requirements had to be met: (1) salespeople had to be recruited to attract retail customers, and (2) working capital had to be raised to rent a warehouse and trucks, purchase and maintain an inventory and finance the establishment of a delivery system capable of processing thousands of individual orders. The single solution to these twin problems employed by Galaxy, i.e., the sale of franchises, is at the heart of the SEC's complaint in this action.

Franchises came in two forms: distributorships and field manager positions. A distributorship originally cost $3,000 but was raised to $5,000 in March 1972, and to $7,000 in October 1972. Field manager positions sold initially for $1,000 but increased to $2,000 in March 1972, and to $3,000 in October 1972.

As explained at meetings held by Galaxy, about which more will be said later, and in manuals produced by the company, distributors and field managers could earn money through Galaxy in two ways, referred to respectively as the retail and wholesale ends of the business.

The retail end of the business involved the actual sale of food to consumers. Distributors were offered a 15% commission on initial customer orders and a 5% commission on reorders. Field managers, in turn, were offered a 10% discount on initial orders and 3% on reorders.

Both distributors and field managers were instructed to hire salespeople to recruit retail customers by offering the salespeople a 5% commission on initial orders and 1% commission on reorders. Franchisees could thus establish sales organizations consisting essentially of salespeople doing the actual "leg work" and yielding the franchisee the difference between the commission received from Galaxy and the lower commission paid the salesman.

The wholesale end of the business refers to the sale of franchises by existing franchisees. Distributors and field managers were encouraged to interest others, called "sponsoring," in purchasing distributorships or field manager positions. A distributor would receive a commission of $1,250, $2,000 or $2,450, depending on the prevailing selling price, for sponsoring a distributor, and $400, $750, or $1,050 for sponsoring a field manager. A field manager could earn $300, $500, or $750, depending on the prevailing franchise selling price, if he sponsored a

distributor or field manager. Additionally, if a field manager sponsored a distributor, his distributor would receive the difference between the prevailing distributor commission, e.g., $1,250, and the commission received by the field manager, i.e., $300. Similarly, if a field manager sponsored another field manager, his distributor would receive the difference between the prevailing field manager commission, e.g., $400, and the commission paid the sponsoring field manager, i.e., $300.[3] Thus, approximately 35-40% of the selling price of franchises was paid as commissions to sponsoring franchisees.

The contract signed by Galaxy franchisees limited the number of distributorships Galaxy could sell to "60 per one million population per state" and specified a quota of 1,079 for New York State distributorships.[4]

Sales of franchises were accomplished through the medium of sales presentations given at "Opportunity Meetings" held by Galaxy. These meetings were held three to four times a week at different hotels in the New York City and Long Island area. Group size at the meetings ranged from as few as 10 to as many as 200.

Lieberman, Horowitz, Roth and Katz were the regular and, for practical purposes, the exclusive speakers at these

meetings. They always spoke from the same prepared text, which had been drafted by them, Rosenthal and Avni. Speakers were not permitted to deviate from the script.

The purpose of the presentation was to explain the Galaxy concept to prospective investors, called "prospects," whom sponsors had brought to the meetings. The speakers also explained in great detail the retail and wholesale commissions to be earned. A blackboard diagram was used to demonstrate how a distributor could earn as much as $60,000 per year from the retail end of the business after only three months in Galaxy.[5] Statements by the speakers relating to how much money one could earn in Galaxy were greeted with cheers and applause by existing franchisees and Galaxy management.[6]

After the first speakers explained the retail and wholesale ends of the business, there was a guest speaker, usually Lee Horowitz or one of the other top Galaxy officials, who promised that Galaxy would itself recruit and distribute to franchisees 8-10,000 retail customers when retail operations began.

Galaxy distributors and managers were instructed to invite prospects to these meetings but to tell them

little or nothing about the Galaxy operation itself. The inducement to attend the meetings was to be simply the opportunity to earn large sums of money. Distributors and managers were told to drive new, expensive automobiles, to wear expensive clothing and to carry large amounts of cash, all to convey to the prospect an illusion of success attributable to association with Galaxy.[7] Once a prospect was lured to a meeting, Galaxy's management did the rest via their established sales presentation.

In addition to Opportunity Meetings, Galaxy held "Sunday Step-Up Meetings",[8] which were designed to obtain commitments, and checks, from the prospects. This process was referred to as "closing the deal" and "getting the check" (GTC", in Galaxy parlance).

At these meetings, which after March 1972 were held in Galaxy's rented warehouse, one speech was given by either Lee, Horowitz, Katz or Roth. Another feature of these meetings, adopted around June 1972 and referred to as "Pay-Day", was the distribution of commission checks to existing franchisees. The one distributing the checks would either call out the amount or ask a prospect to come up and call out the amount. The speaker would usually emphasize that

the franchisees receiving checks had just recently joined Galaxy.

Towards the end of the meeting, prospects were called to the front of the room and asked whether they wished to join Galaxy as a distributor or as a field manager, a question implicit with an assumption. The response was greeted with cheering and applause.

The tremendous exhibitions of enthusiasm at these Opportunity and Step-Up Meetings, the cheering and applauding and the check distributions, were all part of a conscious theme on the part of Galaxy's management to create a high-pressure atmosphere in which the prospect was enveloped and imbued with an almost irrational desire to join—this process was referred to by Lieberman as "jack-up."

Bi-weekly or monthly training sessions were held for new franchisees from October 1971 until July 1973, either at Galaxy's offices or its warehouse. These training sessions were mandatory for distributors. Katz was the principal instructor at these sessions.

The primary focus of the training sessions was the wholesale end of the business. Prospecting techniques such as advertising, approaching friends, relatives and associates

and "cold canvassing"[10] were taught. Practice exercises were conducted and critiqued. Franchisees were taught always to think positively and to be enthusiastic. "Dare to be Great" tapes were played.[11] Franchisees were instructed not to go into any details concerning Galaxy with prospects but only to lure them to the controlled environment of the Opportunity Meetings and to rely on the sales ability of those giving the full organized presentation.

When at Opportunity or Sunday Step-Up Meetings, franchisees were directed to sit next to prospects they had brought there or, if they had come alone, to sit in the back of the room. They were told to applaud new speakers at the meetings, laugh at jokes and generally exhibit constant enthusiasm. Franchisees were encouraged to memorize the script read at Opportunity Meetings.

Franchisees were taught to suggest to prospects ways of raising the necessary funds to purchase a franchise, e.g., borrowing the cash value of insurance policies or taking loans from a bank or finance company. If the prospect was going to take out a loan, franchisees were told to drive the prospect to the lending institution and to tell them to put down furniture as the reason for the loan.

11

Training in the retail end of the business did not begin until the end of November 1971, and was then given in addition to training in prospecting.

Galaxy was run by two management groups, the board of directors and the executive board. The board of directors, which originally consisted of Lieberman, Avni and Rosenthal (who in June 1972 was replaced by Horowitz), actually established operational and management policy and made all important decisions, including the commission percentages to be paid. They were also Galaxy's only corporate officers. The executive board consisted of the three directors and five executive vice-presidents and was a subordinate body whose weekly meetings consisted of discussions of the events of the previous week and decision-making concerning the logistics—location, frequency and speakers—of the Opportunity Meetings and training sessions. The executive board also discussed the content, format and purpose of meetings and training sessions, e.g., the initiation of "pay-day", but it is unclear whether they actually voted on such matters. Only the board of directors could authorize any extraordinary expenditures or promote individuals in the organization. Also, the board of directors could veto any corporate action proposed by the executive board.[12] On

occasion the three directors would leave an executive board meeting to vote on an issue and then report back their decision.[13]

Each member of Galaxy's board of directors received a free distributorship and, from September 1971 until September 1973, an override commission of 3-4% based on total franchise sales.[14] Galaxy's executive vice-presidents apparently received a similar override commission but at a lower percentage rate, i.e., 1/2-1%. Altogether approximately 18% of gross franchise selling prices were distributed to members of the executive board as override commissions. Thus a total of approximately 53-58% of gross franchise sales was paid in various commissions, leaving only 47-42% actually to fund Galaxy.

The organizational arrangement and promotional nature of Galaxy—particularly the concept of non-exclusive franchisees, the Opportunity Meetings and the commission structure—was patterned in large part after that employed by a company called Koscot Interplanetary, Inc. ("Koscot").[15] Lieberman, as well as Galaxy founding fathers, e.g., Avni, Rosenthal and Katz, had been previously associated with Koscot.[16]

Paul J. Deceglie was introduced to Galaxy in the fall of 1971 at a presentation given by Franz Quack to 20 or 30 people at the home of his future in-laws. He subsequently attended an Opportunity Meeting and a Sunday Step-Up Meeting, during which he gave a Galaxy executive a $1,000 check to come in as a field manager and filled out an application. After joining Galaxy, he went tc another Opportunity Meeting in December 1971, which was held in the New York Hilton. No mention was ma[illegible] at any of the meetings attended by him that Galaxy franchises were available only to New York residents. Deceglie is and was during that period a resident of New Jersey and so indicated on the application he filled out. He received mail from Galaxy at his New Jersey address.

In May 1972, Horowitz called him at his home in New Jersey and informed him that there was a problem with his being a New Jersey resident and that he would either have to establish a New York residence or withdraw from Galaxy. He chose to withdraw and received back a check representing his investment.

In the third revision of the script read at Opportunity Meetings dated October 1972, the following

sentence was inserted to be read last by the speaker immediately preceding the guest speaker: "Investments are available only to residents of New York State."

During the summer of 1972, Galaxy adopted a rule, proposed by Katz, which provided that:

> Six months subsequent to the commencement of full scale retail operations, distributors and field managers, regardless of their date of entry into Galaxy's program, will be permitted to exercise Galaxy Foods "final buy-back option". Distributors and field managers will be notified of their option to sell their distributorship back to Galaxy Foods, Inc. at their original purchase price, less any commissions earned. Distributors will be given 30 days from the date of notification to respond to the company offer. A lack of response will be deemed by the company to be a decision to remain on active status with the company. A notification of the desire to exercise the option will be followed by an interview with the company. If the situation cannot be corrected to the satisfaction of both the company and the field manager or distributor, sixty days hence, the buy-back will be executed. The decision shall be binding and final on both parties.

Rule 25 of Galaxy's Rules and Regulations. In conjunction with the adoption of this rule, Galaxy caused to be published in several newspapers of general circulation in New York City advertisements directed at soliciting franchisees which read in part in bold print "A $2,000 or $5,000 guaranteed investment."[17] These advertisements were approved by Galaxy's executive board.

This "guarantee" apparently supplemented or superseded a previous "guarantee", which read:

> Galaxy will do all in its power to commence retail operations. Should the "operating retail territory", (consisting of from 8,000 to 12,000 customers) not have begun operations by June 30, 1973, Galaxy agrees to:
>
> A. If feasible, continue in the effort to establish the first retail foot hold.
> B. Give the option to those individuals who wish to sell their distributorships back to Galaxy, at their original purchase price less commissions paid against it, less ten (10%) percent for handling and interim operating expenses. Those individuals wishing to sell, must notify the company, in writing, after the above-mentioned date. The company will complete the purchase within sixty (60) days after receiving such notification.

Rule 21 of Galaxy's Rules and Regulations.

Lieberman testified that the language of Rule 21 "less commissions paid against it" meant that an investor could get back his original investment less that amount paid as commissions, presumably 53-58%, less 10% for handling or in effect 37-32% of the original amount.

No steps were ever taken, e.g., establishing a sinking fund, to ensure that funds would be available to satisfy either of these "guarantees."

As far back as the fall of 1971, Galaxy announced June 1972 as a target date for the beginning of retail operations,[18] but the target dates were continually readjusted backward as they approached. In a similar fashion, the projected designated retail territory continually shrank. In 1971, prospects and new franchisees were told at Opportunity Meetings and training sessions that the retail territory would consist of a 30-mile radius around each warehouse. In 1972, after the warehouse was actually rented, the operative radius was reduced to ten miles and later in 1972 to three miles.[19]

An article appeared in a local Brooklyn newspaper around September 1972, describing Galaxy in glowing terms and indicating that retail operations were to begin in October. The article also contained the patently false statement that Galaxy then had operations in Long Island, Poughkeepsie, Buffalo and Montreal. Although Galaxy was not responsible for the article's publication, no attempt was made to correct the erroneous statement.

The procedure contemplated by Galaxy when full retail operations began was as follows: A retail customer, living within a three-mile radius of a Galaxy warehouse,

would be contacted by a salesperson (or franchisee) on a door-to-door basis or through advertising. If the retail customer was interested in buying from Galaxy, he or she would be given a catalog and asked to place a minimum $15 order. The initial order would be phoned in to the warehouse by the salesperson (or franchisee). At the warehouse, a Galaxy employee would fill out a form which would be tied into a computer system. The orders would be accumulated in the computer until the end of the day when a high-speed printer would print out copies of the order, one for the "picking" area, one for the truck, one for the distributor, and one for inventory. The computer would also deduct the ordered items from inventory. The orders would be physically filled from shelves in the warehouse and loaded on trucks for delivery. The computer was also to establish a routing sheet for the truck drivers. Finally, the computer was to credit the appropriate franchisees and salespeople with commissions and to cut checks for them. After the initial order, retail customers were to phone in their orders directly to the warehouses.

Galaxy's management estimated a need for twenty warehouses to service the New York City area, assuming only

10% of the population ordered from Galaxy. In addition, it was hoped that each franchisee would maintain an office as a place to hold meetings with his salespeople to monitor their performance.

In November 1972, Galaxy began what is called a "pilot program" to test its retail operation, although none had been mentioned at the time franchises were originally sold. At about this time, Galaxy's management altered the stated retail commission policy by requiring a "cushion" of 8,000 retail customers before paying any commissions on retail sales. Although it appears that Galaxy never acquired more than 4,800 customers, some commissions were paid beginning in March 1973, after vigorous protesting by the franchisees.

In conjunction with the "pilot program" and the expectation of beginning full retail operations, Galaxy purchased over $200,000 worth of food, rented ten delivery trucks, hired as many as ninety-eight employees and spent $150,000 for computer equipment on a lease-purchase basis. During the "pilot program", which lasted from November 27, 1972 until March 31, 1973, Galaxy sold $160,000 worth of goods.

Although the "pilot program" apparently terminated in March 1973, Galaxy continued, and in fact increased its efforts, to recruit new franchisees. The guarantees of Rule 21 and 25 were deleted for franchisees joining after July 1, 1973. The sale of field manager positions ended as of August 1, 1973.

On November 28, 1973, Galaxy filed a voluntary petition in bankruptcy, listing assets of $30,000 and liabilities of $200,000. During the two-year period prior to bankruptcy, Galaxy sold in excess of 800 franchises, raising more than $2.4 million. Aside from the "pilot program", sales of franchises accounted for all of Galaxy's income from inception to demise.

Kirschenblatt

Kirschenblatt was approached concerning employment with Galaxy by Rosenthal and Avni, who offered him a "salaried position." He joined Galaxy in August 1971, and continued until January 12, 1973, when he resigned effective February 1, 1973. He testified that his resignation was prompted by dissatisfaction with Galaxy management, their handling of the retail end of the business, their decision not to pay commissions on retail sales until eight to ten

thousand customers had been acquired, and his consequent belief that the business would not succeed.

Lieberman had met Kirschenblatt at Koscot, where the latter in 1971 purchased a distributorship, which he called K Enterprises. Kirschenblatt sponsored four others into Koscot and received a commission on their sales. He also sold Koscot cosmetic products as well as jewelry, clothing and sundry items to retail customers.

While at Galaxy, he held the position of executive vice-president in charge of marketing, was one of the eight executive board members and regularly attended the weekly meetings, including those at which Galaxy newspaper advertisements were approved. He was not a shareholder, corporate officer or director of Galaxy, but was awarded a distributorship in September or October 1971 for having sponsored two franchisees. He also earned $700 for sponsoring a third franchisee.

His work was directed primarily at making the retail end of the business functional. His duties included the creation and continued up-dating of a catalog of food items with prices to be distributed to Galaxy's retail customers, acting as food buyer for Galaxy and generally

supervising all warehouse activities, e.g., inventory control. His office was located in the Galaxy warehouse.

In his capacity as executive vice-president, he earned a "salary", paid bi-weekly, which was really an override commission of 1/2-1% of total franchise sales. During his tenure at Galaxy, he earned a total of approximately $18-24,000.

He attended as many as 50 to 75 Opportunity Meetings and spoke at least once a month, usually giving the part of the presentation concerning retailing. He also went to twenty-five to thirty-five Sunday Step-Up Meetings, but never spoke at any. He did teach regularly a specified portion of the training sessions given franchisees. He spoke only about retailing and left after completing his presentation.

Although not specifically his function to supervise franchisees, he did assist others in selling franchises at Opportunity and Sunday Step-Up Meetings, both during and after the regular presentations. He was not involved in the preparation of the presentations given at the meetings.

One of the franchisees sponsored by Kirschenblatt, Howard R. Beck, testified that he was driving through the

Queens Midtown Tunnel in August 1971, when he was handed a flyer from a passing car driven by Kirschenblatt. The flyer, which had Kirschenblatt's name and telephone number on the bottom, spoke of the possibility of earning substantial sums of money, having abundant vacation time, working "anywhere in the United States, Puerto Rico, Canada or Mexico . . .", associating "with a man who at age 35 is a multi-millionaire and who will teach you his techniques for accumulating wealth . . ." and being part of "one of the world's fastest growing organizations . . . ."

Beck, attracted by the sums of money mentioned in the flyer, telephoned Kirschenblatt, was told a new concept in food retailing was involved and was invited to a presentation at the Summit Hotel in Manhattan. He went to the meeting, which was attended by 15-20 persons and lasted 30-45 minutes. The speakers were Lieberman, Katz and Horowitz, whose presentations concentrated on how much money could be made in Galaxy. Horowitz wrote the $60,000 figure on the blackboard and people in the back of the room applauded. After the meeting, Kirschenblatt asked him if he understood the presentation, and he told Kirschenblatt he was interested, but wanted to give it some more thought before joining. He subsequently attended another Galaxy

meeting, also in August 1971, held at the Belmont Plaza Hotel and attended by 20-25 people. The format was the same as the prior meeting.

During the week following this last meeting, Kirschenblatt called him and he agreed to come into Galaxy as a field manager. He met Kirschenblatt in Queens in early September 1971 to sign the agreement and to give him a $1,000 check, then the price of a field manager position. Kirschenblatt, however, had with him an application filled out for a distributorship at a purchase price of $3,000. He told Kirschenblatt that he did not have the additional $2,000. Kirschenblatt suggested he obtain a bank loan in that amount, and offered to verify to the bank that he (Beck) was an employee of Kirschenblatt's K Enterprises. Kirschenblatt also suggested he tell the bank the loan was for furniture. Kirschenblatt drove him to the bank and was present when he met a bank officer. The bank refused to make the loan and Kirschenblatt suggested they try a different bank, but Beck refused. The two of them then agreed that Beck would come into Galaxy as a field manager and if he liked the operation, he would elevate later to a distributor position. Kirschenblatt modified the application by crossing out

distributor and $3,000 and inserting field manager and $1,000.

Kirschenblatt's version differs from Beck's. He testified that obtaining the loan was Beck's idea and that all he did was give Beck a "lift" to the bank. He admitted suggesting that furniture was a reason, among others, for the loan. He testified that after Beck left the bank he told him he had decided not to take out the loan.

Kirschenblatt's trial testimony concerning this loan episode is contradicted by his previous testimony before the SEC where he admitted suggesting that Beck take out a loan. His credibility is further undermined by his negative reply to whether he remembered checks being handed out at Sunday Step-Up Meetings, an occurrence he must have witnessed many times. The court credits Beck's version of the loan incident and his testimony in general.

Beck thereafter began working with Kirschenblatt, going to different areas in Brooklyn and Queens to hand out flyers and to do cold canvassing. He did in fact become a distributor in February 1972, and continued in Galaxy for another nine months to a year. During his association with Galaxy, the meetings grew in size to fifty and eventually one hundred guests.

Beck adopted the language of the flyer handed him by Kirschenblatt for his own use, even though he then knew the reference to the 35-year old multi-millionaire to be false and that the same flyer had originally been used by Kirschenblatt in connection with another business, presumably Koscot. He believed that the statements in the flyer, with the exception of the reference to the 35-year old multi-millionaire, did relate to Galaxy.

Beck was never informed prior to joining Galaxy that executives were receiving commission overrides and that some had also been granted franchises for services instead of cash. He was under the impression that the only way Galaxy executives could earn money was by wholesaling themselves.

Beck joined Galaxy because he believed the retail end of the business was a good idea. He worked the wholesale end because at that time it was the only way to earn money in Galaxy, and because he was told that it was necessary to sell franchises in order to get the retail end started.

Shevack

Shevack's introduction to Galaxy appears to have been the result of a coincidence. During June 1972, he went to a catering hall in Brooklyn with a view to renting it. An Opportunity Meeting was underway at the time, and Lieberman, who knew Shevack from Koscot, [20] invited him to join Galaxy. Shevack disclaimed having the requisite $5,000 to purchase a distributorship and Lieberman offered to allow him to "work his way into the business" by sponsoring people through his distributorship and accumulating the resulting commission checks until $5,000 was obtained. Shevack agreed, subsequently sponsored five or six individuals, received $5,000 from Lieberman and purchased his own distributorship with the money in July 1972. Naturally, Lieberman received a commission on that purchase. Lieberman proposed this unusual transaction because of his confidence in Shevack's sales ability and his consequent desire to have him in Galaxy.

Shevack testified that one Peter Cancilla was his partner in the distributorship, that they worked together and split evenly commissions received from Galaxy.

Shevack sold the franchise for $5,500 and left Galaxy sometime between December 1972 and February 1973. He testified that he was dissatisfied with Galaxy's not paying him commissions on retail food orders he had obtained during the "pilot program." During his seven to ten months with Galaxy, he received approximately $11,000 in commissions from franchise sales in addition to the $5,500 he received upon the sale of the franchise.

While at Galaxy, he was not a director, shareholder or officer, nor did he speak at any meetings or have anything to do with the preparation of materials used at those gatherings. He did speak once on prospecting at a training session.

As a prospecting aid, he caused to be printed hundreds of 4-3/4" by 8" cards, which he handed out while cold canvassing. The card began with the question, "are you ready to earn $50,000 per year", continued with "a $2,000 or $5,000 if not totally satisfied guaranteed money back! investment", indicated that New York residents were sought, invited the prospect to an Opportunity Meeting, and contained Shevack's and Cancilla's names and telephone numbers.

Branch Simmons testified that he was approached by Shevack in June 1972, while in his car in Garden City

waiting for a light to change. Shevack asked him if he wanted to make a lot of money, and after receiving an affirmative reply, told Simmons to lead him to the Hempstead Motor Inn. At the Hempstead Motor Inn Simmons attended his first of three or four Opportunity Meetings, after which he joined Galaxy as a field manager for $2,000. He did not have the $2,000, and so, at Shevack's urging and direction, a bank loan was obtained with furniture given as the reason for the loan.

He was influenced to join by the possibility of earning $60,000 or more per year and by Shevack's representations that Galaxy would accumulate and distribute retail customers and that his investment in Galaxy was guaranteed, i.e., that Galaxy would buy back his franchise. He was also impressed by the fact that Shevack was driving an expensive automobile, which the latter led him to believe was atrributable to his association with Galaxy. Shevack also told him that retail operations were to begin during the summer of 1972 and were to include Brooklyn, Manhattan, Upstate New York and Long Island. He was not informed prior to investing that Galaxy management would receive an override commission on all franchise sales. He left Galaxy in March, 1973.

Melvin J. McLean testified that during the summer of 1972, while out on a lunch break, he was asked by Shevack, who had just driven up in a late model car, if he would like to earn $50,000 a year. McLean responded affirmatively, was given Shevack's card (described earlier) and told to come to a meeting that evening. Shevack declined to answer any of McLean's questions, saying he was in a hurry.

McLean went to the meeting that night at the New York Hilton where he heard the regular presentation, including the representation that Galaxy would distribute retail customers to franchisees. Shevack told McLean that he had already made $30,000-40,000 in Galaxy, had purchased a new Cadillac Eldorado and was in the process of buying a new home.

McLean indicated to Shevack that he did not have the funds necessary to purchase a franchise. A few days later, Shevack telephoned him and convinced him to apply for a bank loan, giving as the reason for the loan that it was for furniture and falsely stating that his wife worked for a company in Brooklyn. At this time, McLean worked as a securities clerk for a bank earning $140 per week, already had loans outstanding and was at first reluctant to go along.

but finally succumbed to Shevack's urgings.

The loan was refused but Shevack got McLean to go to Household Finance where he succeeded in borrowing $700. Shevack was waiting in the car for him when he picked up the $700 check, quickly took it from him and had him sign a contract. Shevack told him the money would be given to Galaxy and he would be permitted to pay the $1,300 balance for a field manager position by sponsoring others into Galaxy. He subsequently sponsored two field managers and one distributor, and thus, became a field manager himself. He was also told by Shevack that his investment was completely guaranteed, that is, he was assured of recovering his entire $2,000 investment, less any commissions he received for sponsoring others.

Steven Silverman and his wife testifed that they were introduced to Galaxy in October 1972 by Shevack, who telephoned them at home. He drove them in his Eldorado to an Opportunity Meeting held in the Statler Hilton Hotel. He told them he had purchased the car with money earned through Galaxy. At the meeting the speakers explained the two ways of making money with Galaxy, wholesale and retail. The Silvermans were also told that retail operations were

to begin in several weeks and that there was a provision that they could obtain a refund of their investment, if retail operations did not begin within a specified time. Mr. Silverman invested $7,000 and became a distributor.

The Silvermans did not have the money to invest and so Shevack convinced them to apply to a total of six banks and finance companies. Shevack told them to put down furniture as the reason for the loan and not to mention that loan applications were being filed with other lending institutions. He also gave them a phony W-2 form for Mrs. Silverman, who was not then employed, which reflected income of over $7,000 for 1971, from A & M Dental Labs. Mrs. Silverman had never heard of, much less worked for, such a company. Shevack also gave the Silvermans the name and telephone number of someone at A & M Dental in case further verification was required.

Between October 17 and 26, 1972, the Silvermans borrowed a total of approximately $6,000 from four lending institutions. As each loan check was received, Silverman endorsed it in blank and turned it over to Shevack.

During November 1972, Mr. Silverman was informed that he would be unable to earn any retail commissions until

at least March 1973, because of the "pilot program." Beginning around December 1972, he began requesting a refund of his investment. His requests went unanswered. The Silvermans earned no money in Galaxy.

Shevack categorically denied ever telling anyone to take out a bank loan. He specifically denied ever driving McLean to a bank or assisting him in preparing a loan application. He similarly denied aiding Simmons in any way in connection with borrowing money. Finally, he denied preparing a W-2 for Mrs. Silverman or driving them to six lending institutions.

The court is unable to credit Shevack's testimony on these points. The similarity of Shevack's modus operandi as described by McLean, Simmons and the Silvermans coupled with the fact that this was the same method taught at Galaxy training sessions attended by Shevack, leads inexorably to the conclusion that he did suggest borrowing to these people, that he did drive them to the lending institutions and that he did induce them to give false answers on the loan applications. The court credits the testimony of the Silvermans, McLean and Simmons detailed above despite the fact that their credibility is not enhanced by their having

allowed themselves to be enticed into these questionable acts.

II. Security

The touchstone of the SEC's cause is the existence of a security within the meaning of §2(1) of the Securities Act and §3(10) of the Exchange Act.[21] 15 U.S.C. §§77b(1) and 78c(a)(10). Both sections, which are to be read in pari materia, see Tcherepnin v. Knight, 389 U.S. 332, 335-36 (1967); Glen Arden Commodities, Inc. v. Costantino, 493 F.2d 1027, 1034 n. 6 (2d Cir. 1974), include, in the definition of security, an investment contract. The SEC argues that the franchises sold by Galaxy are investment contracts. Defendants disagree. Their respective contentions must be judged against the backdrop that the securities laws are to be flexibly construed to effectuate their remedial purpose, Tcherepnin v. Knight, supra, 389 U.S. at 337; S.E.C. v. Capital Gains Research Bureau, Inc., 375 U.S. 180, 195 (1963), and that the definition of security:

> "embodies a flexible rather than static principle, one that is capable of adaptation to meet the countless and variable schemes devised by those who seek the use of the money of others on the promise of profits." SEC v. Howey, 328 U.S. 293, 299 (1946).

The obvious starting point of analysis is the Howey case, supra, where the Court found an investment contract to exist where:

> "a person invests money in a common enterprise and is led to expect profits solely from the efforts of the promoter or a third party." 328 U.S. at 299; emphasis supplied.

While a literal reading of the quoted language seems to exclude situations involving an element of investor participation in the profit=making activity, like that here, several Courts of Appeals have held the Court's language to state a rule of inclusion, rather than exclusion. S.E.C. v. Koscot Interplanetary, Inc., 497 F.2d 743 (5th Cir. 1974); S.E.C. v. Glenn W. Turner Enterprises, Inc., 22 474 F.2d 476 (9th Cir.) cert. denied, 414 U.S. 821 (1973). See also, 1050 Tenants Corp. v. Jakobson, 503 F.2d 1375, 1378 n. 5 (2d Cir. 1974); Lino v. City Investing Co., Inc., 487 F.2d 689 (3d Cir. 1973); McCown v. Heidler, 527 F.2d 204, 211 (10th Cir. 1975).

Thus, the use of the word "solely" in Howey, supra, does not foreclose finding an investment contract in situations where there is some investor participation. Instead, the existence of a security turns on an analysis of the

nature and extent of the investors' participation in, and control over, the fate of their investments. While the exact degree of investor participation and control necessary to remove a promotional enterprise from the coverage of the securities laws cannot, because of the virtually limitless permutations of such schemes, be stated in advance, "the efforts by those other than the investor [should be] the undeniably significant ones . . . which affect the failure or success of the enterprise." Koscot, supra, 497 F.2d at 483, quoting from Turner, supra, 474 F.2d at 472. This test is consistent with the purpose of the securities laws "to protect passive, relatively uninformed investors . . . ." Mr. Steak, Inc. v. River City Steak, Inc., 324 F. Supp. 640, 644 (D. Colo. 1970), aff'd in pertinent part, 460 F.2d 666 (10 Cir. 1972).

Here, there are two distinct aspects to the Galaxy concept, the wholesale and retail ends of the business, and the degree of investor participation and control differed with respect to each. Accordingly, they should be analyzed separately. A finding of insufficient investor participation and control concerning either aspect would justify concluding that a security exists. SEC v. United Benefit Life Insurance Company, 387 U.S. 202, 207 (1967).

As concerns the wholesale end of the business, there is no doubt that investor participation was minimal. Galaxy made no attempt to attract only persons with established sales ability. Thus, new franchisees were taught and strictly instructed to do no more than whet a prospect's appetite sufficiently to lure him or her to an Opportunity Meeting. Once there, Galaxy's management, employing a pre-established program in a controlled environment, would accomplish the "hard sell" for which the sponsor would receive the commission.[23] See, Koscot, supra, 497 F.2d at 485.

Nor was the wholesale end of the business an insignificant function to either Galaxy or its franchisees, even though there was evidence that the potential number of franchises which Galaxy would sell in New York was limited to 1,079. In the first place, unless sufficient franchises were sold, the retail end of the business would never get started. Existing franchisees were constantly reminded of this fact by Galaxy's management. Moreover, franchisees knew that until the retail end became operational, the wholesale end was the only way to earn money in Galaxy.

Thus, the court concludes, as did the Turner and Koscot courts, that the investors' efforts relating to the

wholesale end of the business were not "undeniably significant ones"[24] and that accordingly, the sales of Galaxy franchises were the sales of investment contracts within the meaning of the securities laws.

While for practical purposes the analysis could end here, even the retail end of the business involves insufficient investor participation and control to elude the securities laws. While it was possible for franchisees personally to accumulate and service retail customers, the true economic inducement, see SEC v. Joiner Leasing Corp., 320 U.S. 344, 352-53 (1943), was to hire salespeople to accomplish that end and to pocket the commission differential. These salespeople, although technically employees of the franchisee, were in reality employees of Galaxy, which was to register them, train them[25] and pay them.

This finding is supported by the opening statement of the first speaker at the Opportunity Meetings:

> "[I]t is my responsibility . . . to explain how you can earn fantastic sums of money, merely by recruiting salesmen and having them introduce our service to the consumer. Your position would be one of management, for the smart businessman must realize that only as an employer can he ever reach financial success."

As the Court in SEC v. Joiner Leasing Corp., supra, noted:

> "In the enforcement of an act such as this it is not inappropriate that promoters' offerings be judged as being what they are represented to be." Id.

Moreover, the success of any one Galaxy franchisee was inextricably linked to the success of the whole Galaxy operation. Without Galaxy's order-taking, warehousing, packaging, weighing, cutting and delivery services, an individual franchisee could simply not function. Thus, the Galaxy franchisee had no practical control over the success or failure of his own franchise.[26] See Mr. Steak, supra, 324 F. Supp. at 645, and cases cited therein.

This is to be contrasted with a traditional franchisee who can obtain needed raw materials elsewhere and who purchases for the most part only a name and a business style from the franchisor and is thus a relatively independent economic entity. See, e.g., Bitter v. Hoby's International, Inc., 498 F.2d 183, 185 (9th Cir. 1974); Mr. Steak, supra, 324 F. Supp. at 647. The focal point of a traditional franchise is the franchisee's retail outlet; here the center of activity was the Galaxy warehouse. Once

a retail customer was obtained, the customer was to phone the food order directly into Galaxy, which would process and delivery it. No effort on the part of the franchisee was required.[27]

Additionally, a traditional franchisee must usually manage the day-to-day operations of the franchise. Bitter, supra; Nash & Associates, Inc. v. Lum's of Ohio, Inc., 484 F.2d 392, 394-95 (6th Cir. 1973); Mr. Steak, supra, 324 F. Supp. at 642; L.H.M. Inc. v. Lewis, 371 F. Supp. 395 (D.N.J. 1974), aff'd., 510 F.2d 970 (3d Cir. 1975). Here, the Galaxy franchise was almost entirely passive except for the initial recruiting of salespeople and/or retail customers. Cf. Huberman v. Denny's Restaurant, Inc., 337 F. Supp 1249 (N.D.Cal 1972). The recruiting to be done by franchisees was in fact ministerial, not managerial in any true sense, see Mitzner, supra, 358 F. Supp. at 1267-68.[28] Even this aspect was undercut by Galaxy's promise to accumulate on its own, some 10,000 retail customers which it would then distribute to franchisees.[29]

In sum, prospective franchisees were being asked to invest substantial sums of money in Galaxy for which the essence of the consideration received was not products or

otherwise useful training, see Wieboldt v. Metz, 355 F. Supp. 255, 257 (S.D.N.Y. 1973), but simply the opportunity to earn money if the efforts of others, Galaxy's management and the salespeople, proved successful. Offerings of this nature are exactly what Congress intended to subject to the registration and anti-fraud provisions of the federal securities laws.

The court's conclusion that Galaxy franchises were securities is further reinforced by the fact that the one-time franchisee fee paid by investors in Galaxy[30] was the sole contemplated source of its initial working capital. See Hawaii v. Hawaii Market Center, Inc., 52 Hawaii 642, 485 P.2d 105 (1971). By no stretch of the imagination can it be said that the $100 initially invested by Galaxy's incorporators was sufficient to finance the huge inventory and complex delivery system which was needed to render functional the retail end of the business.

Nor can it be said that prospects were being asked to invest in a proven business concept. Cf. Mr. Steak, Inc. v. River City Steak, Inc., supra, 324 F. Supp. at 647. Indeed, Galaxy's own promotional material, which was read at every Opportunity Meeting, proclaimed that the Galaxy concept "could revolutionize the food industry" and described its business objective as "a most unusual joint venture," "still a dream," "a new way of reaching and servicing the

consumer" and "this revolutionary new service."

The speculative nature of the proposed business and the fact that investors were being called upon to provide essentially all of the "turn-key" financing for the entire enterprise marks unmistakably a promotional scheme of the type Congress intended to embrace within the Securities Acts.[31] See, e.g., S.E.C. v. Joiner Leasing Corporation, supra; S.E.C. v. Glen W. Turner Enterprises, Inc. 348 F. Supp. 766, 773 (D. Ore. 1972), aff'd on other grounds, 474 F.2d 821 (9 Cir. 1973).

III. §5 Violations

Section 5 of the Securities Act, 15 U.S.C. §77e,[32] prohibits the sale of a security by any person unless a registration statement is in effect as to that security. The court has found the sale of Galaxy franchises to be the sale of securities and there is no doubt that no registration statement was ever in effect with respect to those franchises. Violations of §5(a) and (c) thus follow automatically, unless some exemption from registration is available.[33]

The burden of establishing the availability of an exemption is on the one claiming it. S.E.C. v. Ralston Purina Co., 346 U.S. 119 (1953); S.E.C. v. Culpepper, 270 F.2d 241, 246 (2 Cir. 1959).

Section 4(1) of the Securities Act, 15 U.S.C. §77d, exempts from the registration requirements of §5 "[t]ransactions by any person other than an issuer, underwriter or dealer . . .". Here, Galaxy itself is undoubtedly an issuer. The primary question is whether Kirschenblatt and Shevack are underwriters.

Section 2(11) defines an underwriter as

> "any person who . . . sells for an issuer in connection with . . . the distribution of any security, or participates or has a direct or indirect participation in any such undertaking . . . ." 15 U.S.C. §77b(11).

Defendants argue that they have not violated §5 because they did not sell any franchises. This argument is premised on the contention that only Galaxy management could actually offer and sell a franchise; sponsors could only invite prospects to the various meetings.

This argument is unpersuasive. Section 2(3) defines "sale" as including "every . . . attempt or offer to dispose of, or solicitation of an offer to buy, a security . . . ." 15 U.S.C. §77b(3) (emphasis supplied). The clear intent of Congress was to embrace a wide range of conduct from initial solicitation or inducement to the actual offer and sale. See S.E.C. v. Chinese Consol. Benev. Assn, Inc., 120 F.2d 738 (2 Cir.), cert. denied, 314 U.S. 618 (1941). The sponsoring activities of Kirschenblatt and Shevack

clearly fall within that embrace.[34] S.E.C. v. Culpepper, supra, 270 F.2d at 247. Certainly, the prospects they lured to Opportunity Meetings were not in such a position vis-a-vis Galaxy that they either had or had access to information with a registration statement would have had to disclose. S.E.C. v. Ralston Purina, supra, 346 U.S. at 125-127.

There was testimony to the effect that Galaxy obtained the opinion of counsel that its franchises were not securities and presumably relied thereon. Even if true, Galaxy's good faith sale of unregistered securities would not be a defense to §5 liability. See SEC v. Guild Films Co., Inc., 279 F.2d 485, 490 (2 Cir.), cert. denied sub nom. Santa Monica Bank v. SEC, 364 U.S. 819 (1960) - "It would be of little solace to purchasers of worthless stock to learn that the sellers had acted 'in good faith'."

Defendants also seem to stress the intrastate exemption of §3(a)(11), 15 U.S.C. §77c(a)(11). Although beginning sometime in 1972, Galaxy did attempt to limit offers to New York residents, prior thereto offers were indiscriminately made and at least one franchise was sold to a New Jersey resident, Deceglie.[35]

> "A basic condition of the [intrastate] exemption is that the entire issue of securities be offered and sold exclusively to residents of the state in question. Consequently, an offer to a

> non-resident which is considered a part of the intrastate issue will render the exemption unavailable to the entire offering." Securities Act Release No. 4434 (December 6, 1961) (emphasis in original).

Here, the entire Galaxy wholesale operation was part of a single plan of financing which continuously offered the same type of investment and thus constituted but one offering. Cf. Shaw v. United States, 131 F.2d 476, 480 (9 Cir. 1942). The intrastate exemption is therefore unavailable to any Galaxy franchise sales, even those sold to New York residents. See SEC v. Van Horn, 371 F.2d 181, 188-89 (7 Cir. 1966); Capital Funds, Inc. v. SEC, 348 F.2d 582, 586 (8 Cir. 1965); SEC v. Hillsborough Investment Corp., 173 F.Supp. 86, 88 (D.N.H. 1958), aff'd, 276 F.2d 665 (1 Cir. 1960); SEC v. Los Angeles Trust Deed and Mortgage Exchange, 186 F. Supp. 830 (S.D. Cal.), aff'd, 285 F.2d 162 (9 Cir. 1960). This is consistent with the fact that whereas §4 exempts transactions, §3 exempts securities.

Accordingly, the court concludes that Kirschenblatt and Shevack are guilty of §5 violations resulting from their sponsoring activities.

Kirschenblatt, moreover, is also liable for §5 violations because of his efforts in assisting others in selling franchises at Opportunity and Step-Up Meetings. Finally, Kirschenblatt, in his role as a Galaxy executive

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(discussed more fully below) is guilty of aiding and abetting Galaxy's §5 violations. See SEC v. Management Dynamics, Inc., 515 F.2d 801, 810-11 (2 Cir. 1975); SEC v. North American R&D Corp., 424 F.2d 63, 81-82 (2 Cir. 1970).

IV. Anti-Fraud Violations

Section 17(a)[36] of the Securities Act, §10(b) of the Exchange Act[37] and Rule 10b-5[38] promulgated thereunder, as judicially construed and applied, mandate fair dealing in the purchase and sale of securities.[39] See SEC v. Capital Gains Research, supra, 375 U.S. at 201

The SEC attributes a host of false statements, actions and omissions to Galaxy in general and to Kirschenblatt and Shevack in particular. Before discussing the more blatant particular misstatements and omissions, it seems clear that the totality of the carnival-type Opportunity and Step-Up Meetings, the "Jack-Up" objective and the "fake it 'til you make it" approach to selling constitutes a manipulative and deceptive device proscribed by §17(a)(1) and (3) of the Securities Act, §10(b) of the Exchange Act and Rule 10b-5(1) and (3). The psychological selling techniques employed by Galaxy successfully duped many innocent, though unwise, investors into parting with funds, often borrowed, which they could ill-afford to invest even in far safer enterprises.

Most apposite to the Galaxy promotional scheme is the following language from the report of the House Committee on Interstate and Foreign Commerce relating to the proposed Securities Act:

> ". . . . $25,000,000,000 worth of securities floated . . . proved to be worthless. These cold figures spell tragedy in the lives of thousands of individuals who invested their life savings, accumulated after years of effort, in these worthless securities . . . . Alluring promises of easy wealth were freely made with little or no attempt to bring to the investors' attention those facts essential to estimating the worth of any security. High-pressure salesmanship rather than careful counsel was the rule in this most dangerous of enterprises."

H.R. Rep. No. 85, 73rd Cong., 1st Sess. p. 2 (1933).

There is evidence in the record that Galaxy's promoters sincerely hoped that the retail enterprise would be successful and that consequently their franchisees would prosper. Nor can it be said efforts were not made to implement the retail end of the business. These factors, however, do not mitigate the fraud perpetrated on the public investors. However strongly the promoters of an enterprise may believe in its potential, prospective investors must still be dealt with fairly and the unadulterated decision to invest or not must be theirs alone. The cornerstone of any contractual arrangement is the agreement of the parties, concluded without overreaching. While the profit of the defrauded may in private litigation absolve the defrauder from damage, in

actions brought to protect the public interest, it is of no moment.

Moreover, any notion of good faith by Galaxy promoters is belied by the huge overrides,[40] totalling 18%, they took notwithstanding that Galaxy had never earned a cent from retail operations.

It would take pages to list all the untruths, half-truths and unrealistic projections and predictions contained in the presentations and literature associated with Galaxy. Among the more frequent and flagrant violations of §17(a)(2) and 10b-5(2) which the court finds established by the evidence are the following:

Misrepresentations

1. An investment in Galaxy was guaranteed.

2. Galaxy would accumulate and distribute 8,000-10,000 retail customers to its franchisees.

3. Galaxy was already operating in New York City, Buffalo, Poughkeepsie, Montreal, Canada and New Jersey.

4. Galaxy would begin retail operations in June 1972.

Omissions

1. Galaxy's management was receiving overrides equalling 18% of gross franchise sales.

2. Certain Galaxy executives had received franchises for "services."

3. None of Galaxy's incorporators or key executives had any managerial experience in the retail food industry.

4. No retail commissions were to be paid during the "pilot program."

Each of the misrepresentations and omissions listed above was material in that a reasonable investor would have unquestionably considered them important in making the decision to invest in Galaxy or not. Affiliated Ute v. United States, 406 U.S. 128, 154 (1972); SEC v. Shapiro, 494 F.2d 1301, 1305-06 (2 Cir. 1974); SEC v. Texas Gulf Sulphur Co., 401 F.2d 833, 849 (2 Cir. 1968) (en banc). Cf. TSC Industries, Inc. v. Northway, Inc., _____ U.S. _____ (June 14, 1976).

While negligence alone suffices as a standard for liability in enforcement proceedings, SEC v. Spectrum, Ltd., 489 F.2d 535, 541 (2 Cir. 1973); SEC v. Manor Nursing Centers, Inc., 458 F.2d 1082, 1096 (2 Cir. 1972); Hanly v. SEC, 415 F.2d 589, 596 (2 Cir. 1969), the misrepresentation and omissions found here were made or withheld either with actual

knowledge or with reckless disregard for the truth.

The evidence reveals that the guarantees were adopted and touted by Galaxy with reckless disregard for its ability to honor them. No sinking fund was established, no insurance taken out and, more importantly, Galaxy officials knew that 53-58% of funds received from franchise sales were being immediately paid out in various commissions, leaving less than 50% for working capital.

Similarly, the projections concerning the commencement of retail operations and the promise to distribute thousands of retail customers were made without regard to Galaxy's ability to realize them. See SEC v. Management Dynamics, supra, 515 F.2d at 809;[41] SEC v. North American R&D, supra, 424 F.2d at 75. The representation relating to the geographical scope of Galaxy's operation was known to be false when made.

While there was no proof in the case that the omissions listed above were deliberately withheld from prospective investors, in view of their obvious importance, the court concludes that the failure to make them known to prospective investors was in reckless disregard of the duty to disclose.

It now remains to discuss the involvement of these particular defendants in the total Galaxy operation and their individual activities in sponsoring others.

Kirschenblatt

Although Kirschenblatt was chiefly responsible for the retail end of the business, his position and activities on the executive board made him a participant in the planning and execution of the Opportunity and Sunday Step-Up Meetings and the organization of the training sessions. Moreover, he continually assisted others in selling franchises at Opportunity and Sunday Step-Up Meetings by explaining to prospects details of the Galaxy program both during and after the presentations. He also taught at the training sessions. There is no question that he had a vested financial interest in the success of the promotional scheme since his "salary" was intimately linked to franchise sales. His involvement in the entire Galaxy operation is clearly sufficient to constitute him an aider and abettor of Galaxy's wrongdoing. SEC v. North American R&D Corp., supra, 424 F.2d at 83; Gross v. SEC, 418 F.2d 103 (2 Cir. 1969). In sum, he associated himself with the venture and by his efforts sought to further it. See SEC v. Coffey, 493 F.2d 1304, 1316 (6 Cir. 1974), cert. denied, 420 U.S. 908 (1975).

Nor can it be said that his participation in the overall fraudulent scheme was merely the result of his failure to exercise due care. Clearly, in view of his prior association with Koscot and his presence at many Opportunity

and Step-Up Meetings, he was surely aware of the many misrepresentations and omissions and the unsavory nature of the fraudulent high-pressure selling being employed.

His sponsoring of three franchisees is also sufficient to charge him with aiding and abetting. By sponsoring others, he both caused them to be exposed to Galaxy's fraudulent conduct and thereby furthered the overall Galaxy promotional scheme.

Finally, he is primarily responsible for anti-fraud violations in connection with his sponsoring of Beck. The flyer used by him in soliciting Beck contained patently false statements, i.e., the possibility of working anywhere in the United States, Canada or Mexico and being taught how to earn large sums of money by a 35-year old multimillionaire, and many half-truths, e.g., the possibility of earning $2,000-$4,000 a month in a relatively short time, as part of one of the world's fastest-growing organizations.

In view of his familiarity with the Galaxy operation and its personnel and his utilization of the flyer from another promotional business, presumably Koscot, the court must conclude that these representations were made either with actual knowledge of their falsity or with reckless disregard for their truth or falsity. Certainly, as the person chiefly responsible for the progress of the

retail operation, he must have realized that there was no possibility of Beck's earning any money, let alone $50,000 a year, from the proposed retail operation for some time.

The misrepresentations in his flyer and his omitting to inform Beck of the commission overrides, a fact of which he was certainly aware, were material in that a reasonable investor would certainly have considered knowing the truth important in deciding on a course of action or inaction.

Shevack

We start with the fact that Shevack was not an officer, director or shareholder of Galaxy and did not speak at Opportunity or Sunday Step-Up Meetings. Nevertheless, his sponsoring of other franchisees thereby deliberately exposing them to the Galaxy "sell-machine", and his having given one training session about prospecting are sufficient to constitute him an aider and abettor of the entire Galaxy operation. In view of his prior position in Koscot, the court must conclude that he was fully aware of Galaxy's fraudulent conduct. Indeed, Lieberman asked him to join Galaxy and offered him a special buy-in arrangement because of his past experience in this type of operation.

Moreover, the evidence clearly reveals that his prospecting and sponsoring activities, which can best be characterized as unscrupulous, are more than sufficient to

establish primary liability for anti-fraud violations. Among the more blatant material false statements which the court finds attributable to him are: (1) his representations to McLean and the Silvermans that he had already earned $30,000-$40,000 in Galaxy and had purchased a new Cadillac Eldorado from those earnings; and (2) his representation to the Silvermans that their investment was completely guaranteed. Although as discussed above, negligence alone is a sufficient standard for liability in enforcement cases, Shevack's misrepresentations were uttered either knowingly or with reckless disregard for their truth or falsity. The conclusion is inescapable, in view of his familiarity with this type of operation, that he must have realized there was little chance of the "guarantees" amounting to anything.

Similarly, he knowingly omitted to inform his prospects that none of Galaxy's executives had any experience in food retailing and that large overrides would be taken out of their investments, facts of which he was certainly aware because of his close relationship with Galaxy and its top officials.

Both defendants argue that even if Galaxy and they did misrepresent the facts to prospects, those misrepresentations were not relied on because the prospects were aware of the true facts before they joined. This argument is supported

to some extent by a disclaimer, reproduced in the margin,[42] which appeared on Galaxy's application form in bold print immediately above the place for the applicant's signature. For the reasons which follow, however, defendants' contention is without merit.

First, the disclaimer addresses itself principally to the fact that Galaxy was not retailing. It does not even begin either to specify any of the material omissions listed above, or to correct misrepresentations concerning the geographical scope of Galaxy's operations, the guarantees, and that no commissions were to be paid during the "pilot program." It certainly did not correct the individual misstatements, discussed above, of Kirschenblatt and Schevack.

Moreover, by the time a prospect was prepared to join, it is unlikely that most, if any, even read the application which was treated by the sponsors as a mere closing formality.

Finally, there is authority for the proposition that reliance is irrelevant in the context of an SEC enforcement proceeding. Cf. SEC v. North American R&D Corp., 424 F.2d at 84; SEC v. Lum's, 365 F. Supp. 1046, 1059 (S.D.N.Y. 1973).[43] Cf. United States v. Ashdown, 509 F.2d 793, 799 (5 Cir. 1975).

V. Injunctive Relief

The SEC argues that given the defendants' past

association with Koscot and Galaxy, and their present connection with a similar business venture, Futuristic Foods, Inc. ("Futuristic"), together with the finding of violations of both the registration and anti-fraud provisions of the securities laws, establishes a clear propensity to violate those statutes and requires a permanent injunction against future violations in the public interest. The court agrees.

Futuristic Foods

The evidence shows that Futuristic was incorporated in January 1973 by Peter Cancilla, Bill Reichert and Shevack. Its purpose is to provide a free home delivery service of supermarket items. Shevack admits he adopted the idea from Galaxy.

Kirschenblatt joined Futuristic in February 1973, after having been asked to do so by Shevack. He is vice-president in charge of administration, earning an annual salary of approximately $20,000. His duties include organizing and implementing the acquiring of retail customers and the purchasing and delivering of food.

Futuristic sells franchises to raise working capital. There are two types of franchises, one for $2,000 (now $3,000) and the other for $5,000 (now $6,000), which entitle the franchisee to different commission percentages on retail food sales and for sponsoring other franchisees.

These franchises were sold at weekday and weekend meetings. The main speakers were Shevack and Cancilla; Kirschenblatt spoke about retailing. The meetings were first held at the company's business offices and later, as the assemblage grew, at hotels. According to Kirschenblatt, these meetings were more businesslike than Galaxy's.[44]

Franchisees were required to attend monthly training sessions, at which Kirschenblatt spoke about retailing.

Apparently Futuristic has actually been operating a retail food business since December 1973, and presently grosses about $20,000 a week. It employs about 60 persons, 30 of whom sell franchises on a fixed salary. It also owns five trucks and rents five others. Price lists are sent to approximately 8,000 customers every two weeks. Retail commissions are, and have been, paid regularly.[45]

With respect to the anti-fraud provisions, there can be no doubt as to the need for a permanent injunction. The court has concluded that both defendants were guilty of anti-fraud violations. "[F]raudulent past conduct gives rise to an inference of a reasonable expectation of continued violations . . .", SEC v. Manor Nursing, supra, 458 F.2d at 1100, and bearing in mind their prior association with Koscot, that inference becomes an irresistible one, see SEC v. Management Dynamics, supra, 515 F.2d at 809, even though they may not have been Galaxy's leading franchise salesmen.

Whether to enjoin future violations of the registration provisions presents a somewhat more difficult question. Although the court has held Galaxy franchises to be securities, it can hardly be said that the question was free from doubt. The seminal appellate case, Turner, supra, was not decided until February 1, 1973, months after both defendants had left Galaxy. Moreover, there is evidence in the record that Galaxy had obtained the opinion of counsel that the federal security laws were not being violated.

The court is nonetheless persuaded, in view of their association with Futuristic, that an injunction against future violations of the registration provisions is also warranted. The defendants, according to their own testimony, are actively involved in Futuristic which, until enjoined by another court, was selling franchises facially similar to those sold by Galaxy and Koscot. This involvement stretches back to January 1973 and covers a period during which the Turner and Koscot decisions were handed down. Whether Futuristic franchises are securities is not for this court to decide. They are, however, sufficiently similar[46] to indicate that defendants have a conscious propensity to disregard the registration provisions. The SEC has thus demonstrated "a reasonable likelihood of future violations." SEC v. Manor Nursing, supra, 458 F.2d at 1101. See also SEC v. Shapiro, supra, 494 F.2d at 1308; SEC v. Management Dynamics, supra,

515 F.2d at 807.

Accordingly, the defendants are to be permanently enjoined from violating the registration or anti-fraud provisions of the securities law with respect to the sales of any securities in the form of franchise or distributorship interests. Cf. NLRB v. Express Publishing Company, 312 U.S. U.S. 426, 435 (1941).

VI. Disgorgement

The SEC seeks disgorgement of all benefits received by the defendants to deter future violations by these defendants and others and to ensure that they do not profit from their past wrongdoing. This the court has power to do, SEC v. Manor Nursing, supra, 458 F.2d at 1103-04, as long as the relief is remedial, not punitive, in nature. SEC v. Texas Gulf Sulphur Company, 446 F.2d 1301, 1308 (2 Cir. 1971).

Kirschenblatt

As explained earlier, Kirschenblatt's primary role in Galaxy involved the retail end of the business and there is evidence that during his approximately one and one-half years with Galaxy he worked full-time and long hours in that connection. The court has concluded that he knowingly aided Galaxy's many violations of the securities laws and that his "salary" was determined by the number of franchises sold. While not desiring to sanction his conduct in this area, the

the court believes that under the circumstances it would be inequitable to order him to fully disgorge the $18,000 - $24,000 he was paid in his capacity as a Galaxy executive. He did, however, benefit unjustly by receiving without payment a distributorship for which other investors had to pay $3,000 in 1971. Accordingly, it is equitable to require him to disgorge the value of that distributorship. Additionally, his sponsoring of McLean into Galaxy constituted the direct exposure of another to the fraudulent promotional scheme and also included serious misrepresentations. Accordingly, Kirschenblatt is ordered to disgorge $3,700 representing the $700 McLean commission and the value of the distributorship he received.

Shevack

Shevack testified he received in essence a total of $16,500 for sponsoring others and that half of that sum went to his partner, Cancilla. The court will accept his testimony on these figures and order that he disgorge $8,250.

Based on testimony which the court credits and which was detailed above, it appears that Shevack was both relentless and unscrupulous in his selling activities. It is important to the administration of the securities laws that he not benefit from those illegal actions.

Shevack testified that he devoted full time to Galaxy while associated with it. From this the court is presumably to draw a distinction between his case and those cases where courts have ordered disgorgement of profits earned through stock transactions without real personal effort. The court concludes, without much difficulty, that working hard at defrauding others provides not a distinction but an additional basis for finding disgorgement to be proper.

The parties shall confer and settle an order in accordance with this opinion on ten (10) days' notice from the date hereof.

SO ORDERED.

Edward R. Neaher

U. S. D. J.

Dated: Brooklyn, New York
July 26, 1976

FOOTNOTES

1 Pending resolution of this matter on the merits, all individual defendants consented to some form of preliminary restraint.

2 When Rosenthal left Galaxy in June 1972, Horowitz replaced him on the board and became secretary-treasurer, Avni became president and Lieberman became vice-president and chairman of the board.

3 An existing field manager could elevate to a distributor by paying the prevailing price differential between the two types of franchises and appropriate commissions would be paid out of this differential.

4 Lieberman explained the derivation of this ratio as follows:

> "If there are, in fact, 20,000,000 people in New York State, we broke it down and said, what is a very comfortable living for somebody? Well, we were offering a figure of $60,000 a year. That is a pretty comfortable living. So in order to earn $60,000 a year, a person would have to earn in excess of $1,000 a week. So we did it on a basis of 60 distributorships per million people, or 250,000 familes, which, at a 10 per cent saturation and $25 a week per family in food purchases, would amount to $1666 a week per distributor in earnings, which is in excess of $60,000 a year." Tr. 588-89.

5 The word "could" is emphasized because the script obviously was carefully drafted to avoid making an explicit representation.

6 Although Galaxy's management had at first decided against cheering at the meetings, they later acquiesced in the decision of then existing Galaxy franchisees to put more enthusiasm in the meetings.

7 A similar procedure employed by the Turner organization was referred to as "fake it 'til you make it." Glen W. Turner Enterprises, Inc. v. SEC, 474 F.2d 476, 480 (9 Cir. 1973).

8 The transcript incorrectly refers to these gatherings as "Set-Up Meetings".

9 Rule 23 of Galaxy's Rules and Regulations provided: "Distributor agrees to complete the basic business management course within seventy-five (75) days of registering with the company. Should the distributor not complete said training, any commissions earned after the seventy-five (75) day period may be withheld by Galaxy until such time as the course is completed."

10 Cold canvassing refers to soliciting total strangers almost anywhere, e.g., on the street, at crowded train stations.

11 Dare to be Great was the name of a subsidiary of Glen W. Turner Enterprises, Inc. See Securities and Exchange Commission v. Glen W. Turner Enterprises, Inc., 348 F. Supp. 766 (D. Ore. 1972), aff'd, 474 F.2d 476 (9 Cir.), cert. denied, 414 U.S. 821 (1973).

12 For example, the executive board voted to put to the distributors the question of whether to reduce to 900 from 1079 the number of New York franchises Galaxy would sell. The distributors voted to reduce but the board of directors vetoed the reduction.

13 As explained by Lieberman:

> "[C]orporate officers could sign checks. Corporate officers could demand decisions made the way they ruled. Corporate officers could fire executives. Corporate officers could virtually run the business without the executive board." Tr. 458.

14 Several Galaxy officials, Lieberman, Horowitz, Katz and Roth, were also granted the privilege of operating

automobiles leased by Galaxy.

15 See SEC v. Koscot Interplanetary, Inc., 497 F.2d 473 (5 Cir. 1974).

16 Lieberman's title at Koscot was Assistant State Director for Wholesale for Manhattan and his duties included supervising meetings at which people were introduced to Koscot and assisting franchisees in recruiting others. He received a commission based on all Manhattan franchise sales.

17 A similar advertisement approved by Galaxy appeared in the Buffalo Evening News in August 1972. These advertisements indicated that New York residents were desired, although a similar advertisement appearing in a Spanish newspaper did not limit the solicitations to New York residents.

18 A memorandum from Kirschenblatt to Galaxy franchisees dated March 10, 1972 referred to the fast approaching retail target date.

19 Shevack testified that the delivery area "changed on a daily basis."

20 Shevack owned a Koscot distributorship with his brother and was Assistant State Director for Brooklyn at the same time Lieberman was Assistant State Director for Manhattan. He was not an officer, director or shareholder of Koscot.

21 Section 2(1) reads:

> "(1) The term 'security' means any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, or, in general,

> any interest or instrument commonly known as a 'security', or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing."

22 In United Housing Foundation, Inc. v. Forman, 95 S.Ct. 2051, 2060 n. 15 (1975), the Court noted the Turner construction of the word "solely" in the Howey opinion but expressed no view as to its correctness. In Parvin v. Davis Oil Company, 524 F.2d 112, 116 n. 2 (9 Cir. 1975), the Ninth Circuit noted the United Housing Foundation, supra, opinion and went on to apply the Turner construction of Howey.

23 Lieberman testified that

> "They [new franchisees] were told in training sessions to be enthusiastic, to applaud the speakers who came up because, after all, we felt that speakers were taking a great burden of doing a lot of work for them by not making them go through the presentation before each one of these individuals. In effect, they were working for them." Tr. 371; emphasis supplied.

24 The defendants apparently concede as much.

> "62. The conduct of a franchisee in relation to the solicitation of additional franchisees was nothing more than the performance of a ministerial act." Defendants' Proposed Findings of Fact, ¶62.

25 Compare Lino v. City Investing, supra, where the court upheld a lower court's determination that the franchise agreement in question was not a security. In Lino, the defendant would contract with a franchisor seeking to market its products. The defendant would also enter into agreements with licensees (franchisees) who were to recruit area distributors to represent the franchisor;

the area distributor was, in turn, required to recruit sub-franchisees who would actually market the franchisor's products. Plaintiff licensee (franchisee) under the contract with the franchisor was obligated to devote his "full time and best efforts" to the enterprise and was obligated not only to recruit but actually to train area distributors working under him. Since the licensee (franchisee) was to receive certain percentages of the fees paid to the defendant by area distributors and their sub-franchisees, all of the licensee's (franchisee's) profits were, in large measure, to be derived either directly or indirectly from the training and promotional program established by the licensee himself.

26 This factor also serves to satisfy the common enterprise criterion of the Howey test. 328 U.S. at 299.

27 See Mitzner v. Cardet International, Inc., 358 F. Supp. 1262 (N.D. Ill. 1973), where the court refused to dismiss a complaint predicated on a franchise arrangement being a security even though the franchisee actually took the retail order, transmitted it to the franchisor, received the goods from the franchisor and delivered them to the retail customer.

28 It was contemplated that franchisees must hold periodic meetings with their salespeople to supervise their productions, but this could hardly consume more than a few hours a month.

29 A Galaxy flyer, extolling the benefits of Galaxy's contemplated retail operation, stated: "Satisfaction is guaranteed by Galaxy Foods, not the independent distributor . . . ."

30 As contrasted with a traditional franchise where the franchisor's "financial participation was unlimited, and [he] remained liable for continuing operational expense." Mr. Steak, Inc. v. River City Steak, Inc., supra, 324 F. Supp. at 645.

31 It is thus unnecessary to decide whether the Galaxy franchises were profit sharing agreements or securities in the traditional sense as urged by the SEC.

32 Section 5(a) and (c) provide:

> "(a) Unless a registration statement is in effect as to a security, it shall be unlawful for any person, directly or indirectly - (1) to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to sell such security through the use or medium of any prospectus or otherwise; or (2) to carry or cause to be carried through the mails or in interstate commerce, by any means or instruments of transportation any such security for the purpose of sale or for delivery after sale. * * *
> (c) It shall be unlawful for any person, directly or indirectly, to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to offer to sell or offer to buy through the use or medium of any prospectus or otherwise any security, unless a registration statement has been filed as to such security, or while the registration statement is the subject of a refusal order or stop order or (prior to the effective date of the registration statement) any public proceeding or examination under section 77 of this title." 15 U.S.C. §77e.

33 There was ample evidence that Galaxy made extensive use of the jurisdictional means, i.e., mails, telephones and newspapers, in conducting its prospecting activities. The individual defendants also used the telephones in soliciting others. See Lennerth v. Mendenhall, 234 F. Supp. 59, 63 (N.D. Ohio 1964).

34 See SEC v. Management Dynamics, Inc., 515 F.2d 801, 810 (2 Cir. 1975), request for stock quotation and breadth of market held solicitation of an offer to buy sufficient to sustain §5(c) violation. See also SEC v. Culpepper, supra, 270 F.2d at 246, where, in apposite language the court said, referring to the §4 exemption:

> "It does not in terms or by fair implication protect those who are engaged in steps necessary to the distribution of security issues. To give Section 4(1) the construction urged by the defendant would afford a ready method of thwarting the policy of the law and evading its provisions."

35 Another franchisee, Werner Kunst, listed his address on his Galaxy field manager application dated 2/20/72 as Hamburg-Schenefeld, Germany. Galaxy was obviously aware of Kunst's German residence because by document dated 12/31/71, he was appointed First Assistant Vice-President of European Operations and allotted $800 to conduct research on the feasibility of Galaxy operating in Europe. Kunst paid $2,000 more and became a distributor on May 22, 1972.

Lieberman's testimony that no application for a franchise by a non-New York resident was ever accepted is simply untrue.

36 Section 17(a) states: "(a) It shall be unlawful for any person in the offer or sale of any securities by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, directly or indirectly - (1) to employ any device, scheme, or artifice to defraud, or (2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or (3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser." 15 U.S.C. 77(q)(a).

37 "§78j. Manipulative and deceiptive devices. It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange - . . . (b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors." 15 U.S.C. §78j.

38 Rule 10-b5 C.F.R. Section 240.10-5 (1970): "It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange, (a) To employ any device, scheme, or artifice to defraud, (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, - in connection with the purchase or sale of any security."

39 Use of jurisdictional means need be only slight. Here, as indicated earlier, Galaxy clearly made extensive use of mails, telephones, etc. The individual defendants also made sufficient use of the telephones in selling franchises to establish this court's jurisdiction as to their primary violations, even though there may have been no fraudulent statements made over the phone. See Hilton v. Mumaw, 522 F.2d 588, 602 (9 Cir. 1975); Kerbs v. Fall River Industries, Inc., 502 F.2d 731, 737-38 (10 Cir. 1974); Lawrence v. SEC, 398 F.2d 276, 279 n. 2 (1 Cir. 1968); Myzel v. Fields, 386 F.2d 718, 727 (8 Cir. 1967),

cert. denied, 390 U.S. 951 (1968); Heyman v. Heyman, 356 F. Supp. 958, 969 (S.D.N.Y. 1973); Dupuy v. Dupuy, 511 F.2d 641, 642-43 (5 Cir. 1975); Aquionics Acceptance Corp. v. Kollar, 503 F.2d 1225 (6 Cir. 1974); Roe v. United States, 316 F.2d 617, 621 (5 Cir. 1963), where the court said:

> "[C]ircumstances might be such that a jury could conclude that in a high pressure sales campaign, the promoters thought it was wise to allay apprehension of those who had repurchased by a continuation of reassuring literature. Likewise, such material would be admissible in showing any one or more or all of the uses of the mails in the course of bringing about the sale as ultimately consummated." Id.

This language is apposite here. Cf. United States v. Ashdown, 509 F.2d 793, 799-800 (5 Cir. 1975).

40 For example, it appears that Lieberman was paid about $90,000 during his tenure with Galaxy.

41 The language of the court in Management Dynamics, supra, is most apt:

> "[T]he impression [was given] that the project was virtually certain to be completed, when the hurdles to development were so formidable that it was in fact little more than an idea in which the developers had faith." Id.

42 "(B) APPLICANT ACKNOWLEDGES THAT:
(1) GALAXY, PRESENTLY, IS NOT RETAILING, FOODS OR OTHER SUPERMARKET ITEMS.
(2) GALAXY IS A STARTING COMPANY AND IT MAY NEVER DEVELOP TO THE POINT WHEREBY DISTRIBUTORS MAY EARN PROFITS, SALARIES OR COMMISSIONS FROM THE SALE OF SUCH ITEMS.

(3) APPLICANT UNDERSTANDS THAT HIS/HER INVESTMENT WITH GALAXY IS A HIGH RISK INVESTMENT, HOWEVER, APPLICANT HAS DETERMINED SUCH INVESTMENT, ALTHOUGH WITH RISK, IS A SOUND VENTURE INVESTMENT WITH A NEW AND EMERGING COMPANY, POSSESSING A HIGH POTENTIAL FOR SUCCESS."

43 Additionally, as concerns the material omissions, reliance is presumed. Affiliated Ute, supra, 406 U.S. at 153-54; Handwerger v. Ginsberg, 519 F.2d 1339, 1342 (2 Cir. 1975).

44 Since August 23, 1974, franchisees are not permitted to sell franchises by order of Judge Conner of the Southern District Court.

45 These general statements concerning Futuristic are not intended to be conclusive on any factual issues to be resolved in the action pending before Judge Conner.

46 Shevack himself testified that Futuristic is a copy with modifications of Galaxy which was in turn an offshoot of Koscot.

FINAL JUDGMENT OF PERMANENT INJUNCTION AGAINST DEFENDANTS SHEVACK AND KIRSCH.

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

SECURITIES AND EXCHANGE COMMISSION Plaintiff, -against- GALAXY FOODS, INC. ARTHUR LIEBERMAN a/k/a ARTY LEE RALPH AVNI CHARLES HOROWITZ BRUCE KATZ STEVEN ROTH MARK GLAZER IRWIN DONALD KIRSCHENBLATT a/k/a DONALD KIRSCH GEORGE PADILLA ARTHUR SHEVACK Defendants.	73 Civ. 1742 (ERN) FINAL JUDGMENT OF PERMANENT INJUNCTION AGAINST DEFENDANTS ARTHUR SHEVACK AND DONALD KIRSCH

Plaintiff Securities and Exchange Commission ("Commission"), having filed its complaint in this action on November 26, 1973, and defendants Donald Kirsch a/k/a Donald Kirschenblatt ("Kirsch") and Arthur Shevack ("Shevack") having acknowledged service of a copy of the Summons and Complaint herein, having entered a general appearance, having filed answers thereto, and this Court having jurisdiction of the subject matter of this action and the parties, and a trial on the merits

FINAL JUDGMENT OF PERMANENT INJUNCTION AGAINST DEFENDANTS SHEVACK AND KIRSCH

having been held before this Court in this matter, and this Court having issued an opinion in this matter dated July 26, 1976, and there being no just reason for delay in the entry of this Judgment, it is hereby

ORDERED, ADJUDGED AND DECREED that the defendants Kirsch and Shevack, their agents, servants, employees, successors, assigns, attorneys and those persons in active concert or participation with them and each of them be and hereby are permanently enjoined from

A. Directly and indirectly

1. making use of any means or instruments of transportation or communication in interstate commerce or of the mails to offer to sell, through the use or medium of any prospectus or otherwise, the securities of Galaxy Foods, Inc. ("Galaxy"), or any other securities, unless and until a registration statement has been filed with the Commission as to such securities or while a registration statement filed with the Commission as to such security is the subject

of a refusal order or stop order of the Commission (prior to the effective date of the registration statement) or any public proceeding or examination under Section 8 of the Securities Act of 1933, as amended, ("Securities Act"), 15 U.S.C. 77h;

2. making use of any means or instruments of transportation or communication in interstate commerce or of the mails to sell the securities of Galaxy, or any other securities, unless and until a registration statement is in effect with the Commission as to such securities; and

3. carrying the securities of Galaxy, or any securities to be issued by said corporation, or any other securities, or causing such securities to be carried through the mails or in interstate commerce by any means or instruments of transportation for the prposes of sale, or delivery after sale, unless and until a registration statement is in effect with the Commission as to such securities.

Provided, however, that nothing in the foregoing portion of this permanent injunction shall apply to any security which is exempt from the provisions of Section 5 of the Securities Act, 15 U.S.C. 77e.

B. Directly and indirectly

1. in connection with the offer for sale, sale, offer to purchase or purchase of securities of Galaxy, or any other securities, making use of any means or instruments or instrumentalities of transportation or communication in interstate commerce or of the mails to: (i) employ any device, scheme or artifice to defraud; (ii) engage in any transaction, practice or course of business which operates or would operate as a fraud or deceit upon any purchaser, prospective purchaser, seller, or prospective seller, or (iii) obtain money or property by means of or to make untrue or misleading statements of material facts or to omit to state a material fact, necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading.

FINAL JUDGMENT OF PERMANENT INJUNCTION AGAINST DEFENDANTS SHEVACK AND KIRSCH

IT IS FURTHER ORDERED that within 10 days of the entry of this Judgment, as set forth in the opinion of this Court dated July 26, 1976, defendant Kirsch shall disgorge and pay into the registry of this Court the sum of three thousand seven hundred dollars ($3,700) and defendant Shevack shall disgorge and pay into the registry of this Court the sum of eight thousand two hundred and fifty dollars ($8,250) plus, in the case of each defendant, lawful interest of six per cent (6%) computed from November 26, 1973 to the date of payment on an annual compounded basis. Such payments made by defendant Shevack and defendant Kirsch are to be disposed of as this Court, by separate order, shall direct.

IT IS FURTHER ORDERED that this Court shall retain jurisdiction of this matter for all purposes and to make such further orders as may appear appropriate to this Judgment and its enforcement.

S/ Edward R Neaher
UNITED STATES DISTRICT JUDGE

Dated: New York, New York
~~August~~ September 13, 1976

JUDGEMENT ENTERED:

S/ Lewis Orgel
CLERK
By S/ Marilyn Glen

A TRUE COPY
ATTEST
DATED September 22 76
BY Mary Anne Grant

NOTICE OF APPEAL.

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

X

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

- against -

GALAXY FOODS, INC.
ARTHUR LIEBERMAN a/k/a ARTY LEE
RALPH AVNI
CHARLES HOROWITZ
BRUCE KATZ
STEVEN ROTH
MARK GLAZER
IRWIN DONALD KIRSCHENBLATT a/k/a
DONALD KIRSCH
GEORGE PADILLA
ARTHUR SHEVACK,

Defendants.

X

NOTICE OF APPEAL

73 Civ. 1742

(ERN)

S I R S :

Notice is hereby given that IRWIN DONALD KIRSCHENBLATT, a/k/a DONALD KIRSCH and ARTHUR SHEVACK, defendants above named, hereby appeal to the United States Court of Appeals, for the Second Circuit from the Final Judgment of Permanent Injunction, entered against them in this action on the 13th day of September, 1976, and this appeal is from each and every part of said judgment as well as the whole thereof.

GOIDEL, GOIDEL & HELFENSTEIN, P.C.
Attorneys for Defendants KIRSCH & SHEVACK
Office & P.O. Address
127 John Street
New York, New York

BY:

A Member of the Firm.